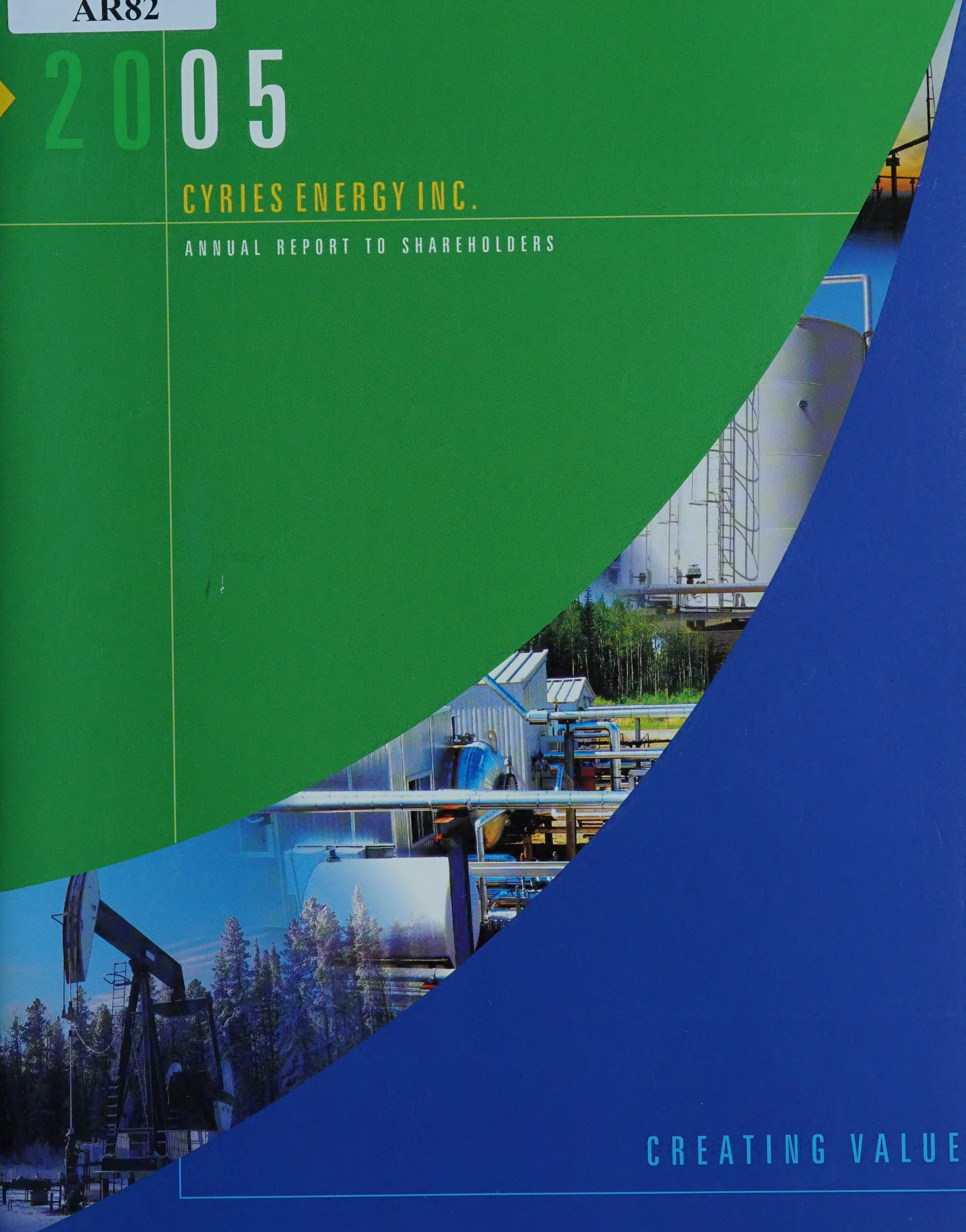
2005

CYRIES ENERGY INC.

ANNUAL REPORT TO SHAREHOLDERS



CREATING VALUE

Cyries Energy Inc. is an oil and natural gas exploration and development company, actively engaged in the acquisition, development, exploration for and production of oil and natural gas reserves primarily in the province of Alberta.

ANNUAL AND SPECIAL MEETING OF SHAREHOLDERS

Tuesday, May 16 at 3:00 pm (Calgary time)
Devonian Room, Calgary Petroleum Club 319 - 5th Avenue SW,
Calgary, Alberta

Cyries Energy Inc. invites all shareholders to attend the annual meeting. Shareholders not able to attend are encouraged to sign and return the Form of Proxy.

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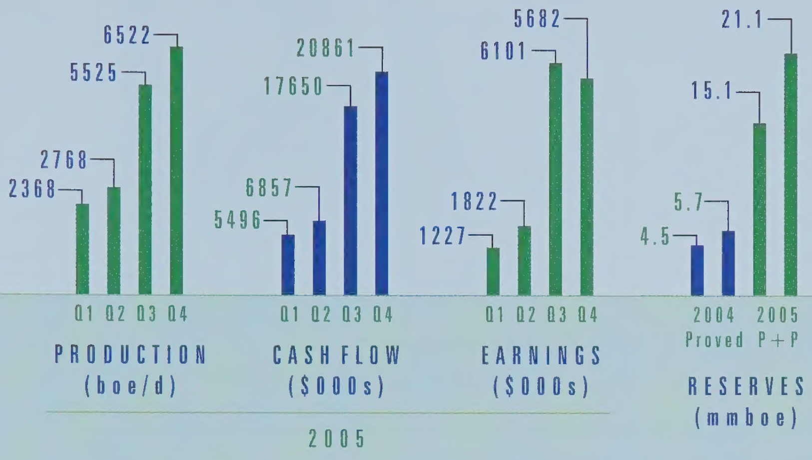
FINANCIAL HIGHLIGHTS



(000s, except as indicated)	*Three months ended December 31,* 2005	2004	% Change	*Year ended December 31,* 2005	*Period ended December 31,* 2004[(1)]	% Change
Petroleum and natural gas sales	**42,419**	6,834	521	**96,415**	11,352	749
Net earnings	**5,682**	1,171	385	**14,832**	1,551	856
Per share basic	**0.14**	0.05	180	**0.46**	0.07	557
Per share diluted	**0.13**	0.04	225	**0.41**	0.06	583
Cash flow from operations	**20,861**	3,783	452	**50,864**	5,951	755
Per share basic	**0.53**	0.16	231	**1.58**	0.25	532
Per share diluted	**0.48**	0.14	243	**1.40**	0.22	536
Capital expenditures	**37,821**	16,670	127	**101,591**	32,558	212
Acquisitions	**-**	-	-	**125,229**	-	nm
Bank debt and working capital deficiency	**73,220**	9,313	686	**73,220**	9,313	686
Weighted average shares outstanding						
Basic	**39,259**	24,218	62	**32,286**	23,646	37
Diluted	**43,640**	27,756	57	**36,416**	27,084	35
Average sales price						
Oil *($/bbl)*	**64.35**	52.05	24	**64.22**	51.28	25
Natural gas *($/mcf)*	**12.14**	7.19	69	**10.17**	7.06	44
NGL *($/bbl)*	**61.19**	42.62	44	**55.23**	43.11	28
Total *($/boe)*	**70.69**	45.19	56	**61.28**	44.69	37
Average daily production						
Oil *(bbl)*	**1,166**	382	205	**772**	358	116
Natural gas *(mcf)*	**29,975**	7,041	326	**19,905**	5,830	242
NGL *(bbl)*	**360**	88	309	**221**	66	235
Total *(boe)*	**6,522**	1,644	297	**4,311**	1,396	209
Production expenses *($/boe)*	**8.01**	7.11	13	**7.62**	6.94	10
Operating netback *($/boe)*	**42.51**	28.34	50	**36.93**	27.04	37
Undeveloped land						
Gross acres	**230,833**	70,803	226	**230,833**	70,803	226
Net acres	**172,497**	49,876	246	**172,497**	49,876	246
Farm-in acreage *(net acres)*	**26,800**	53,512	(50)	**26,800**	53,512	(50)

(1) Period from July 2, 2004 to December 31, 2004.

TO OUR SHAREHOLDERS

Donald F. Archibald
Chairman and Chief Executive Officer

We are proud of the success achieved by Cyries Energy Inc. in 2005. By December 31, 2005, we had completed a full eighteen months in business. In 2005, we have accomplished these results:

- *Average production in 2005 increased 209 percent to 4,311 barrels of oil equivalent per day, compared to with 1,396 boe per day during the period from July 2, 2004 to December 31, 2004. Production per diluted share increased 361 percent during the same period.*

- *Fourth quarter 2005 production averaged 6,522 boe per day, compared with 1,644 in the fourth quarter of 2004, an increase of 297 percent. Production per diluted share increased 152 percent for the same period.*

- *Funds generated from operations were $50.9 million ($1.40 per share diluted) compared with $5.9 million ($0.22 cents per share diluted) for the prior year. This represents a 755 percent increase and a 536 percent increase on a per share basis.*

- *Net earnings for the year were $14.8 million (41 cents per share diluted), compared with $1.5 million (6 cents per share diluted) for the prior year. This represents an 856 percent increase and a 583 percent increase on a per share basis.*

We have consistently applied Cyries' planned strategy for growth. We maintain an aggressive drilling program and, periodically, layer in strategic acquisitions. Our results demonstrate Cyries' success in building a diverse and productive asset base, a strong balance sheet and engaging a management team with proven operational and technical depth.

BUILDING AN ASSET BASE

Cyries is primarily a natural gas producer with assets that are located in northwestern Alberta.

Cyries commenced operations in July 2004, with assets concentrated in the Deep Basin/Peace River Arch areas. During 2005, we successfully expanded our presence in these two core areas and added three new core areas to diversify our portfolio. Through both drilling and acquiring, we added to our asset base in Rainbow Lake, Hotchkiss and Marten Hills/Judy Creek. We primarily focus on the Deep Basin/Peace River Arch because, in this area, we have experience and have achieved success, both for Cyries and for our predecessor company, Cequel Energy Inc. Medium depth drilling targets, multi-zone potential, and, mostly, natural gas prospects are the characteristics that attracted us to this region and that keep us focused here. Our technical expertise in the Deep Basin/Peace River Arch area, as well as a large existing undeveloped land base, converge to provide Cyries with a competitive advantage.

During 2005, Cyries added production and acreage at Rainbow Lake, Hotchkiss and Marten Hills/Judy Creek. These three new core areas further diversify our asset base and become elements of a broader platform from which Cyries will grow in the future. At Rainbow Lake, our drilling strategy has three primary targets: shallow natural gas in the Bluesky and the Jean Marie zones and crude oil in the Keg River zone. At Hotchkiss, we target shallow natural gas in the Debolt/Shunda zones. At Marten Hills/Judy Creek, we target several zones but, primarily, shallow natural gas in the Wabiskaw.

We will continue to drill to expand our prospects and production in all of these areas and, at the same time, to pursue property and corporate acquisitions that enhance our current assets and maintain our growth. We will combine exploration and development drilling with higher risk, higher reward targets in the Deep Basin/Peace River Arch. We will complement this strategy with multi-year resource development projects in our other core areas.

ACHIEVEMENTS

Drilling

Cyries achieved a drilling success rate of 80 percent in 2005. This rate is consistent with our strong performance in previous reporting periods and reflects both the technical proficiency of our exploration group and the multi-zone potential targeted by much of our drilling.

In 2005, Cyries spent approximately $100 million on drilling 64 wells (42.9 net), acquiring land and building related facilities. In 2006, we expect to spend approximately $130 million to drill up to 100 wells. Our 2006 drilling program will target 40 percent exploration locations and 60 percent development locations. We expect about half of 2006 drilling will be for shallow wells (less than 1200 metres in depth), as we expand our shallow natural gas projects. The remainder of 2006 drilling anticipates targeting wells at depths of about 2,500 metres, primarily in the Deep Basin.

Acquisitions

Two acquisitions completed in 2005, Devlan Exploration Inc. and a private company, have proved very beneficial to Cyries. They provided three new core areas and added to our Deep Basin/Peace River Arch assets.

Subsequent to the completion of these acquisitions, we have extended existing plays, made exploration discoveries, added to our undeveloped land base through Crown land sales and farm-ins and proved up additional reserves beyond what was evaluated at the time of purchase.

Financial performance

We focus our financial strategy for growing Cyries on cost control, competitive reserves additions, high netbacks and maintaining a strong balance sheet. In 2005, Cyries delivered solid performance in controlling costs while growing production per share more than 300 percent since the first quarter of operations, increasing cash flow per share growth by approximately 500 percent and earnings per share by more than 1,200 percent.

We preserved Cyries' strong balance sheet in 2005 by holding debt, including working capital deficit, to about $73 million at year-end. We kept debt at this conservative level despite spending about $227 million in capital in 2005 or, approximately $125 million on acquisitions and $102 million for drilling and related activities.

OUTLOOK

During 2005, Cyries successfully built a foundation of four producing core areas, anchored by our Deep Basin/Peace River Arch assets. Cyries intends to continue growing in 2006 by exploiting this diverse range of assets with drilling and, potentially, through further acquisitions.

Despite rising costs throughout the industry, Cyries maintains an efficient cost structure which produces high netbacks and achieves an economic recycle ratio.

Our 2006 capital expenditures program will increase to $130 million, excluding possible acquisitions. This represents a 30 percent increase when compared to 2005 capital expenditures. We expect to fund this program from cash flow and our balance sheet, while continuing to deliver attractive growth per share.

Cyries enters 2006 with confidence, assured that we can achieve our goals by utilizing our competitive advantages of technical expertise and a large undeveloped land base.

In reporting our 2005 success and looking forward to achieving continued positive performance in 2006, it is a pleasure to extend my appreciation to Cyries' employees for their dedication, to our directors for their experience and guidance and, to our shareholders for their continued support.

On behalf of the Board of Directors,

Donald F. Archibald
Chairman and Chief Executive Officer
March 15, 2006

Donald F. Archibald
Chairman and
Chief Executive Officer

Mike Kabanuk
Vice President,
Operations and
Chief Operating Officer

Brendan Carrigy
Vice President,
Exploration

Gary Peddle
Vice President,
Business Development

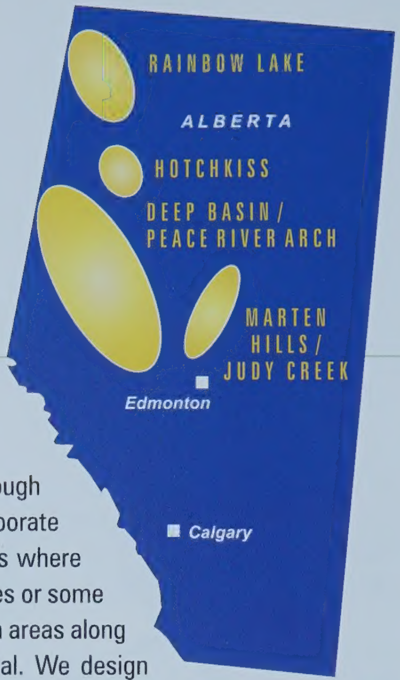
Tom Emerson
Vice President,
Land

Richard Thompson
Vice President,
Geophysics

Dave Gillis
Treasurer

Erin Thorson
Chief Financial Officer
and Controller

REVIEW OF OPERATIONS



In 2005, Cyries successfully executed a strategy focused on growth through exploration and development drilling, property acquisitions and corporate acquisitions. Our focus, with respect to drilling, is to concentrate in areas where Cyries has a competitive advantage due to technical expertise, land, facilities or some combination of these factors. We mitigate drilling risk by exploring in known areas along established geological trends, and, in formations with multi-zone potential. We design Cyries' drilling program to take advantage of our expertise and concentrated land base in the Deep Basin/Peace River Arch, Rainbow Lake, Hotchkiss and Martin Hills/Judy Creek areas of the province of Alberta. The geological formations we target range from the Doe Creek at 1,200 metres to the Wabamun at 3,400 metres. There are approximately ten potential producing horizons between these two depths.

Cyries' strategy proved to be successful in 2005. In the year, our drilling activity resulted in 64.0 wells (42.9 net) drilled with an 80 percent success rate and an average working interest of 67 percent. The following table summarizes the results our 2005 drilling program.

	Exploration		***Development***		***Total***	
(wells drilled)	***Gross***	***Net***	***Gross***	***Net***	***Gross***	***Net***
Natural gas	23.0	15.9	18.0	13.2	41.0	29.1
Oil	1.0	0.5	10.0	4.5	11.0	5.0
Dry	7.0	5.6	5.0	3.2	12.0	8.8
Total	31.0	22.0	33.0	20.9	64.0	42.9

As a result of our drilling success and corporate acquisitions, average production has grown from 1,142 boe/d in the first quarter of operations to 6,522 boe/d in the fourth quarter of 2005. Cyries continues to focus on natural gas and 77 percent of 2005 production was natural gas. We expect to continue this weighting toward natural gas at approximately the same rate throughout 2006. The following table summarizes our average daily production in each core area.

Core area	***Natural gas*** *(mcf/d)*	***Crude oil and NGL*** *(bbls/d)*	***Total*** *(boe/d)*
Deep Basin/Peace River Arch	14,909	618	3,103
Rainbow Lake	437	175	248
Hotchkiss	1,092	-	182
Martin Hills/Judy Creek	3,467	200	778
Total	19,905	993	4,311

Cyries acquired 42,700 acres (net) of land as part of the Plan of Arrangement with Cequel Energy Inc. and Progress Energy Ltd. We added an additional 157,000 acres (net) of land since inception through acquisitions, land sales and farm-in agreements.

Cyries employs a selective land acquisition strategy, whereby we aggressively pursue acquisitions and farm-in agreements on prospects with previously identified drilling opportunities. Our objective is to retain capital by minimizing the amount of land inventory with no near term exploration prospects. We expect prospects associated with Cyries' current undeveloped land inventory to provide over 85 drilling locations and 25 contingent locations through to the end of break-up in 2007.

In addition, we have identified numerous follow-up opportunities from Cyries' drilling success in 2005 and early 2006. The multi-zone nature of our land position increases the potential for follow-up drilling opportunities as the multiple zones provide several new prospect leads. There are opportunities for additional drilling locations through both downspacing and infill drilling on a number of our existing producing properties.

DEEP BASIN/PEACE RIVER ARCH

Cyries' Deep Basin/Peace River Arch core area is generally characterized as having medium-depth, multi-zone properties prone to delivering high quality natural gas and light oil. With the existing well-established infrastructure, this is a desirable region of the Western Canada Sedimentary Basin. Cyries' Deep Basin/Peace River Arch drilling program largely drove our successful 2005 production volumes. We drilled a total of 49 wells (34.6 net) in the Deep Basin/Peace River Arch in 2005. New wells are drilled to an average depth of 2,100 metres, produce at approximately 1,500 mcf per day and cost an average of $1.7 million to drill and complete. Cyries has approximately 68,000 acres (net) of undeveloped land in the Deep Basin/Peace River Arch area.

In the Deep Basin/Peace River Arch, we have drilled eight successful wells in the first quarter of 2006. We anticipate drilling a total 50 wells here in 2006.

RAINBOW LAKE

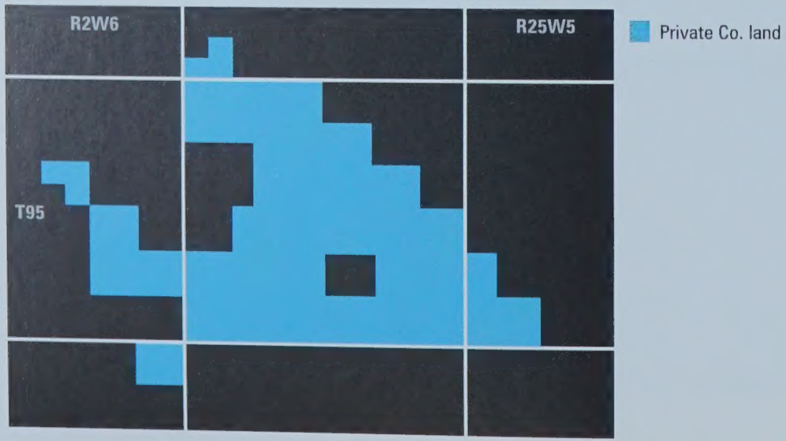
Cyries' Rainbow Lake area is generally characterized as having medium-depth, multi-zone properties prone to delivering high quality natural gas and light oil with established processing infrastructure. The Rainbow Lake property was acquired in July 2005 as part of the Devlan acquisition, and for the remainder of 2005, we drilled a total of 5 wells (3.5 net) in the Rainbow Lake area. New wells targeting the Jean Marie formation are drilled to an average depth of 1,200 metres, produce at approximately 75 boe per day and cost an average of $1.4 million to drill and complete. Cyries has approximately 44,000 acres (net) of undeveloped land in the Rainbow Lake area.

In the Rainbow Lake area, we have drilled and cased seven wells in the first quarter of 2006. We anticipate drilling an additional five wells here in the remainder of the year.

HOTCHKISS

Cyries' Hotchkiss area is generally characterized as having shallow-depth, multi-zone properties prone to delivering high quality natural gas. The Hotchkiss property was acquired in August 2005 as part of the 1181608 Alberta Ltd. acquisition. New wells are drilled to an average depth of 750 metres, produce at approximately 300 mcf per day and cost an average of $600,000 to drill and complete. Cyries has approximately 5,500 acres (net) of undeveloped land in the Hotchkiss area.

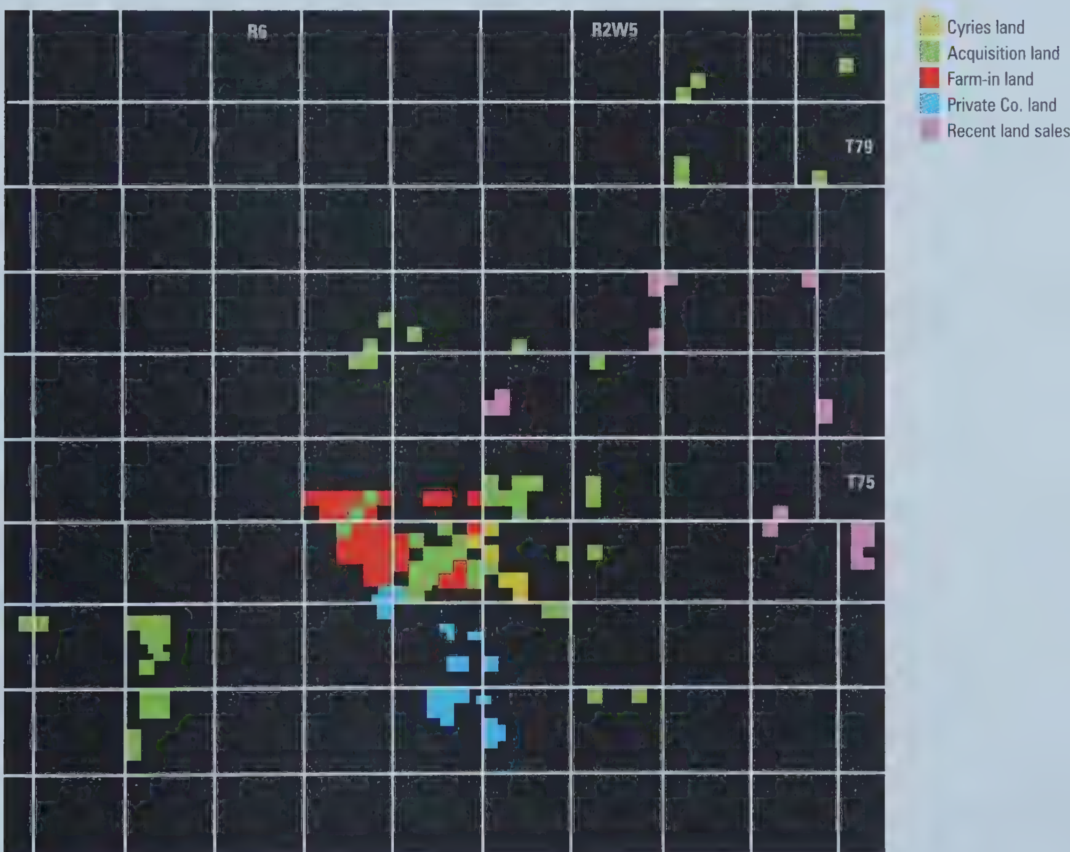
In the Hotchkiss area, we have drilled and cased four wells in the first quarter of 2006. We anticipate drilling at least two additional wells here in the remainder of the year.



MARTEN HILLS/JUDY CREEK

Cyries' Marten Hills/Judy Creek area is generally characterized as having medium-depth, multi-zone properties prone to delivering high quality natural gas and light oil. We drilled a total of 10 wells (4.9 net) in the Marten Hills/Judy Creek area in 2005. New wells are drilled to an average depth of 700 metres, produce at approximately 300 mcf per day and cost an average of $400,000 to drill and complete. Cyries has approximately 45,500 acres (net) of undeveloped land in Marten Hills/Judy Creek area.

In the first quarter of 2006, we have drilled four successful wells. We anticipate drilling a total of five wells here in 2006.



Based on an independent qualified reserves evaluation conducted by Gilbert Lausten Jung Associates ("GLJ") effective December 31, 2005, Cyries had proved reserves of 15.1 mmboe and proved plus probable reserves of 21.1 mmboe. Compared with December 31, 2004, proved reserves increased 236 percent from 4.5 mmboe, and proved plus probable reserves increased 270 percent from 5.7 mmboe.

Seventy eight percent of proved reserves are classified as proved producing and 76 percent of probable reserves are associated with reserves that are currently producing. Approximately 76 percent of Cyries' reserves are natural gas on a 6:1 boe conversion basis.

The reserves data set forth below (the "Reserves Data") is based upon an evaluation by GLJ Petroleum Consultants ("GLJ") with an effective date of December 31, 2005 and dated March 8, 2006 ("GLJ Report") in accordance with National Instrument 51-101 Standards of Disclosure of Oil and Gas Activities. The Reserves Data summarizes our crude oil, natural gas liquids and natural gas reserves and the net present values of future net revenue for these reserves using constant prices and costs and forecast prices and costs. The estimates of reserves are subject to judgements of future events for which actual results may vary materially. Disclosure of the Corporation's oil and natural gas reserves is contained in the Annual Information Form filed at www.sedar.com.

SUMMARY OF OIL AND GAS RESERVES BASED ON FORECAST PRICES AND COSTS [1]

	Light and medium oil		*Natural gas*		*Natural gas liquids*		*Total*	
	Gross *(mbbl)*	***Net*** *(mbbl)*	***Gross*** *(mbbl)*	***Net*** *(mbbl)*	***Gross*** *(mmcf)*	***Net*** *(mmcf)*	***Gross*** *(mboe)*	***Net*** *(mboe)*
Proved developed producing	1,995	1,806	54,586	39,578	691	464	11,784	8,866
Proved developed non-producing	571	473	12,119	9,088	203	141	2,794	2,128
Proved undeveloped	115	99	2,444	1,731	13	9	535	397
Total proved	2,681	2,378	69,149	50,397	907	614	15,113	11,391
Total probable	1,104	950	27,063	19,862	397	269	6,011	4,530
Total proved plus probable	3,785	3,328	96,212	70,259	1,304	883	21,124	15,921

(1) Using GLJ's January 1, 2005 price forecast.

NET PRESENT VALUES OF FUTURE NET REVENUE BASED ON FORECAST PRICES AND COSTS

Cyries reserves were evaluated using GLJ's price forecast effective January 1, 2006 prior to provision for interest and general and administrative expenses. The after tax scenario is based on the company's estimated December 31, 2005 tax pools. It should not be assumed that the discounted net present value estimated by GLJ represents the fair market value of the reserves.

($000s)	Before deducting income taxes Discounted at 0%	5%	10%	15%	20%	After deducting income taxes Discounted at 0%	5%	10%	15%	20%
Proved developed producing	355,827	291,417	252,115	224,989	204,774	284,250	232,316	200,585	178,672	162,353
Proved developed non-producing	94,274	75,043	63,093	54,952	49,022	61,990	48,985	40,910	35,417	31,423
Proved undeveloped	11,973	10,370	9,097	8,066	7,219	7,841	6,614	5,657	4,894	4,274
Total proved	462,074	376,830	324,305	288,007	261,015	354,081	287,915	247,152	218,983	198,050
Total probable	178,678	117,121	87,533	70,131	58,615	118,561	77,169	57,288	45,600	37,869
Total proved plus probable	640,752	493,951	411,838	358,138	319,630	472,642	365,084	304,440	264,583	235,919

The January 1, 2006 pricing forecasts presented below apply to the Company. The information therein has been prepared by GLJ. These prices have been utilized in determining the reserves and net present value noted above.

SUMMARY OF PRICING AND INFLATION RATE

	Light and medium crude oil			Natural gas	Natural gas liquids		
Period	WTI Cushing Oklahoma ($US/bbl)	Edmonton par price 40° API ($Cdn/bbl)	Cromer Medium 29.3° API ($Cdn/bbl)	AECO C-Spot gas price ($Cdn/bbl)	Edmonton Pentanes Plus ($Cdn/bbl)	Inflation rate (%/year)	Exchange rate ($US/$Cdn)
2002	26.08	40.33	35.48	4.04	40.73	2.2	0.637
2003	31.07	43.66	37.55	6.66	44.23	2.8	0.721
2004	41.38	52.96	45.75	6.88	54.07	1.8	0.768
2005 (estimate)	56.60	69.11	57.07	8.58	69.45	2.2	0.825
2006 Q1	56.00	65.25	52.25	10.45	66.00	2.0	0.850
2006 Q2	56.00	65.25	56.00	10.35	66.00	2.0	0.850
2006 Q3	57.50	67.00	58.25	10.45	67.75	2.0	0.850
2006 Q4	58.00	67.50	56.75	11.05	68.25	2.0	0.850
2006 Full Year	57.00	66.25	55.75	10.60	67.00	2.0	0.850
2007	55.00	64.00	55.25	9.25	65.25	2.0	0.850
2008	51.00	59.25	51.25	8.00	60.50	2.0	0.850
2009	48.00	55.75	48.25	7.50	56.75	2.0	0.850
2010	46.50	54.00	46.75	7.20	55.00	2.0	0.850
2011	45.00	52.25	45.25	6.90	53.25	2.0	0.850
2012	45.00	52.25	45.25	6.90	53.25	2.0	0.850
2013	46.00	53.25	46.00	7.05	54.25	2.0	0.850
2014	46.75	54.25	47.00	7.20	55.25	2.0	0.850
2015	47.75	55.50	48.00	7.40	56.50	2.0	0.850
2016	48.75	56.50	48.75	7.55	57.75	2.0	0.850
2017+	+2%/yr	+2%/yr	+2%/yr	+2%/yr	+2%/yr	2.0	0.850

RESERVES ADDITION COSTS

Reservse addition costs for 2005 (including the change in future development capital) were $19.37 per boe proved and $14.31 per boe proved plus probable. Excluding changes in future development capital reserves addition costs were $18.67 per boe proved and $13.40 per boe proved plus probable.

Cyries generated an operating netback of $36.93 per boe in 2005. The recycle ratio in 2005 was 1.91 times on a proved basis and 2.6 times on a proved plus probable basis.

Reserves addition costs related to drilling and exploration activities were $17.55 per boe proved and $12.57 per boe proved plus probable. Reserves addition costs related to acquisitions were $21.29 per boe proved and $16.40 per boe proved plus probable.

($000s, except as indicated)	*Capital costs*	*Change in future development costs*	*Total costs*	*Reserves additions*	*Finding, development and acquisition costs($)*
Including the effect of acquisitions					
Proved	226,820	8,517	235,337	12,151	19.37
Proved plus probable	226,820	15,349	242,169	16,928	14.31
Excluding the effect of acquisitions					
Proved	101,245	8,517	109,762	6,253	17.55
Proved plus probable	101,245	15,349	116,594	9,273	12.57
Acquisitions					
Proved	125,575	-	125,575	5,898	21.29
Proved plus probable	125,575	-	125,575	7,655	16.40

The Board of Directors is responsible for the stewardship of Cyries and for overseeing the business of the Company. The Company is committed to the highest standards for its corporate governance practices and procedures. Specifically, the Board's responsibilities include:

> *reviewing and approving significant strategic, operating and capital initiatives;*
> *identifying and managing the principle risks of Cyries;*
> *assessing senior management;*
> *succession planning;*
> *developing Cyries' approach to corporate governance;*
> *approval of communications policies;*
> *assessing the adequacy of internal controls and management systems;*
> *approval of the annual and quarterly financial statements; and*
> *reviewing and approving annual capital budgets and management compensation.*

The Board is comprised of eight members of whom six are deemed to be "independent" pursuant to applicable securities laws. The Board meets quarterly at minimum and participates in the annual strategic planning session to review and approve corporate objectives.

2005 CORPORATE GOVERNANCE INITIATIVES

In 2005, the Board undertook a number of initiatives to improve its corporate governance practices. These are as follows:

> *A Code of Business Conduct (the "Code") was implemented which sets out standards of ethical behaviour for the Company's directors, officers, employees and consultants. The Code can be found on the Company's website at www.cyries.com and is filed on Sedar at www.sedar.com.*
> *A Whistleblower policy was introduced to ensure that the Company can maintain a workplace where concerns regarding questionable business practices can be raised without fear of discrimination, retaliation or harassment.*
> *A Nominating Committee was established which will assess and make recommendations as to the size, composition and effectiveness of the Board and its committees.*
> *Douglas Dafoe, an independent director, was appointed as Lead Director. The Lead Director provides independent leadership to the Board and maintains communication with all members of the Board and the committee chairs to optimize the effectiveness of the Board and its committees. In this regard, the Lead Director ensures that the Board is alert to its obligations to the Corporation and its shareholders, reviews conflict of interest issues with respect to members of the Board and chairs "in camera" meetings of the Board, without management present, at every Board meeting.*
> *Position descriptions were created for the role of Chairman and Chief Executive Officer. The Chairman of the Board and Chief Executive Officer, being Donald Archibald, is not an independent director. In his role as Chief Executive Officer, Mr. Archibald is responsible for developing and implementing the Company's short and long-term goals, maintaining a high level of integrity in the Company and managing the day-to-day affairs of the Company. In his role as Chairman of the Board, Mr. Archibald provides leadership to the Board to act as an effective team in carrying out its duties and responsibilities and ensures that all required business is brought before the Board to enable it to carry out its duties.*

COMMITTEES OF THE BOARD

The Audit Committee, Reserves Committee and Compensation Committee, together with the recently formed Nominating Committee, assist the Board in discharging its duties. Specific duties and responsibilities have been documented and approved for each of the committees of the Board. All of the committees of the Board are comprised of independent directors.

Audit Committee

The Audit Committee is comprised of three independent directors, being Douglas Dafoe, Chairman, Fred Coles and Max Muselius. The Audit Committee assists the Board in fulfilling its responsibilities with respect to the integrity and completeness of the annual and quarterly financial statements; compliance with accounting and finance based legal requirements; ensuring the independence of the external auditor; and reviewing accounting systems and procedures. The members of the Audit Committee have direct access to the external auditors. The Chair of the Committee is a Chartered Accountant.

Reserves Committee

The Reserves Committee is comprised of three independent directors, being Fred Coles, Chairman, Howard Crone and Douglas Dafoe. The Reserves Committee reviews the selection of the company's independent reserves engineers, as well as the reserves estimates and evaluations prepared by these engineers. The Committee also reviews the methodologies used by the independent engineers and the reliability of the information provided. The Chairman of the Reserves Committee is a professional engineer and was formerly a principal for an independent reserves evaluation firm.

Compensation Committee

The Compensation Committee is comprised of three independent directors, being Geoffrey Cumming, Chairman, Alison Jones and Max Muselius. The Committee reviews executive compensation matters, key human resources policies and the compensation program for the company including bonuses.

Nominating Committee

The Nominating Committee is comprised of three independent directors, being Geoffrey Cumming, Chairman, Max Muselius, and Alison Jones. The Nominating Committee is responsible for recommending to the Board new candidates for election to the Board, for determining the competencies and skills the Board considers necessary for the Board, as a whole, to possess and for reviewing the comprehensive orientation and training of new and existing directors.

THE BOARD OF DIRECTORS

Donald F. Archibald

Mr. Archibald has been the Chairman and Chief Executive Officer of Cyries since May 27, 2004; prior thereto Mr. Archibald was the President and Chief Executive Officer of Cequel Energy Inc. from January 2002 to June 2004; prior thereto Mr. Archibald was the President and Chief Executive Officer of Cypress Energy Inc. from 1995 to 2001.

Fred C. Coles

Mr. Coles has been the president of Menehune Resources Ltd. a private company, since April 2002; prior thereto Mr. Coles was the Executive Chairman and Chairman of the Board of Applied Terravision Ltd.

Howard Crone

Mr. Crone has been an independent businessman since June 2004; prior thereto Mr. Crone was the Vice President, Corporate Development and Chief Operating officer of Cequel Energy Inc. from January 2002 to June 2004; prior thereto Mr. Crone was the VP Operations and Chief Operating Officer of Cypress Energy Inc. from 1995 to 2001.

Geoffrey A. Cumming

Mr. Cumming has been the Vice Chairman and Chief Executive Officer of Gardiner Group Capital Limited and Garbell Holdings Limited, private Canadian investment companies, since October 1994.

Douglas A. Dafoe

Mr. Dafoe has been the Chairman and Chief Executive Officer of Ember Resources Inc., a public coal bed methane company, since July 2005; prior thereto Mr. Dafoe was the President and Chief Executive Officer of Thunder Energy Inc., a public oil and natural gas company, from October 1995 to July 2005.

Alison Jones

Ms. Jones has been an independent businessperson since July 2004; prior thereto Ms. Jones was the Vice President, Exploration of Cequel from January 2002 to June 2004; prior thereto Ms. Jones was the Vice President, Exploration of Cypress Energy Inc., a public oil and gas company, from 1995 to March 2001.

Max Muselius

Mr. Muselius has been a Rancher in Southern Alberta and British Columbia since January 2000; prior thereto Mr. Muselius was the Executive Chairman of Ensite Incorporated, a technology company, from January 1999 to December 1999.

Gary Peddle

Mr. Peddle has been the Vice President, Business Development of Cyries since June 28, 2004; prior thereto Mr. Peddle was the Vice President, Land of Cequel from January 24, 2002 to June 2004; prior thereto Mr. Peddle was the Vice President, Land of Cypress Energy Inc., from June 1998 to March 2001.

This management's discussion and analysis ("MD&A") contains operating and financial information for 2005 and 2004. The comparative financial information in this report comprises only the operating results for Cyries Energy Inc. ("Cyries") for the period from July 2, 2004 to December 31, 2004 (the "Period" or the "Comparative period"). As a result, comparisons to prior year will be expressed on a per barrel of production basis where possible. The MD&A should be read in conjunction with the financial statements for the year ended December 31, 2005. This MD&A is dated as of March 15, 2006.

Cyries was incorporated under the Business Corporations Act (Alberta) on May 20, 2004 and commenced operations July 2, 2004. On July 2, 2004 as a result of a plan of arrangement involving Cequel Energy Inc. ("Cequel"), Progress Energy Ltd. ("Progress"), Progress Energy Trust (the "Trust") ProEx Energy Ltd. ("ProEx") and Cyries, certain oil and gas properties were transferred to Cyries from Cequel in exchange for common shares of Cyries.

***BOE presentation** - Per barrel of oil equivalent ("boe") amounts have been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil ("6:1"). The reader should be aware that historical results are not necessarily indicative of future performance. All values are presented in thousands, other than boe and per share amounts.*

***Non-GAAP measurements** - Cyries evaluates performance based on net income, operating netback and cash flow from operations. Cash flow from operations, which is expressed before changes in non-cash working capital and site restoration expenditures, is used by the Company to analyze operations, performance, leverage and liquidity. Operating netback is a benchmark used in the oil and gas industry to measure the contribution of oil and natural gas sales following the deduction of royalties, production expenses and transportation costs. Cash flow from operations and operating netback do not have a standard meaning prescribed by Canadian Generally Accepted Accounting Principles ("GAAP") and therefore may not be comparable to other companies.*

***Forward-looking statements** - This MD&A contains forward-looking statements. Forward-looking statements are based on current expectations that involve a number of risks and uncertainties that could cause actual events or results to differ materially from those reflected in the MD&A. Forward-looking statements are based on the estimates and opinions of Cyries' management at the time the statements were made.*

DESCRIPTION OF BUSINESS

Cyries is an oil and natural gas exploration company, actively engaged in the acquisition, development, exploration for and production of oil and natural gas reserves primarily in the Province of Alberta. The Company's primary operating areas include the Deep Basin/Peace River Arch, Hotchkiss and Rainbow Lake areas of northwestern Alberta and the Marten Hills area of central Alberta.

Cyries' strategy for growth was highlighted in 2005 through aggressive drilling programs coupled with strategic acquisitions. Cyries' has been successful in building a strong and diversified asset base, a strong balance sheet and a management team with operational and technical strength. This asset platform will enable Cyries to continue to grow in 2006 through a combination of drilling and acquisitions.

The financial strategy for growing Cyries has focused on cost control, competitive reserves addition costs, high netbacks and a strong balance sheet. Despite rising costs in the industry, Cyries has maintained a good cost structure that produces high netbacks and results in economic exploration and development costs.

Business environment

In 2005 high oil and gas prices contributed to strong cash flows and earnings for the oil and gas industry operating in the Western Canada Sedimentary Basin. As a result, drilling activity and well completions reached historically high levels during the year. The emergence of several new industry players increased competition for undeveloped lands and producing properties in Cyries' core areas. The pace of drilling activity, high commodity prices, and increased demand for land and services resulted in an increase in related costs in 2005 along with the costs of operating producing properties.

Summary

($000s, except per share data)	*Year ended December 31, 2005*	*Period ended December 31, 2004[1]*
Total revenues	**96,415**	11,352
Net income	**14,832**	1,551
Net income per share - basic	**0.46**	0.07
Net income per share - diluted	**0.41**	0.06
Total assets	**364,230**	69,711
Bank debt	**47,249**	3,092
Working capital deficiency	**25,971**	6,220

(1) Represents the period from July 2, 2004 to December 31, 2004.

The year ended December 31, 2005 was highlighted by sustained high oil and natural gas prices resulting in increases to revenue and net income compared to the same period in 2004. Net income per share increased 557 percent to $0.46 per share for the year ended December 31, 2005 compared with $0.07 in the comparative period.

During the year the company executed a $100,000 capital program and completed two corporate acquisitions for total consideration of $125,229. Drilling success and production added through acquisition increased average production to 4,311 boe per day in 2005 from 1,396 boe per day in the comparative period.

On July 1, 2005 the Company closed the acquisition of Devlan Exploration Inc., a public oil and gas company. The transaction was completed by way of a Plan of Arrangement ("Arrangement") involving Cyries Energy Inc., Devlan Exploration Inc. ("Devlan") and Dual Energy Inc. ("Dual"). Cyries issued an aggregate of 8,558 common shares and assumed approximately $22,500 of Devlan net debt. In addition, certain Devlan assets and $4,500 of debt were transferred to Dual, a newly formed oil and gas company. The acquisition added approximately 2,300 boe/d of production.

On August 12, 2005 the company closed the acquisition of 1181608 Alberta ULC, a privately owned oil and gas company, for cash consideration of $57,000. The acquisition added approximately 1,300 boe/d of production.

DETAILED FINANCIAL ANALYSIS

Petroleum and natural gas production

	Year ended December 31, 2005	*Period ended December 31, 2004*
Oil *(bbls/d)*	**772**	358
Natural gas *(mcf/d)*	**19,905**	5,830
Natural gas liquids *(bbls/d)*	**221**	66
Total *(boe)*	**4,311**	1,396

Production for the year ended December 31, 2005 increased 209 percent to 4,311 boe/d from 1,396 boe/d in the comparative period. The increase from the prior year is due to the production added through drilling and the two corporate acquisitions. The Devlan acquisition closed July 1, 2005, adding approximately 2,300 boe/d of production for the remaining six months of the year. The acquisition of 1181608 Alberta ULC on August 12, 2005 resulted in an increase of approximately 1,300 boe/d. The production acquired through acquisition is approximately 79 percent natural gas.

Natural gas production for the year ended December 31, 2005 increased to 19,905 mcf/d compared to 5,830 mcf/d for the period ended December 31, 2004. Oil and liquids production for the year ended December 31, 2005 increased to 993 barrels per day compared to 424 barrels per day for the period ended December 31, 2004.

Revenue

($000s, except as indicated)	*Year ended December 31, 2005*	*Period ended December 31, 2004*
Revenue		
Oil	**18,091**	3,341
Natural gas	**73,867**	7,489
Natural gas liquids	**4,457**	522
Total	**96,415**	11,352
Average sales price		
Oil *($/bbl)*	**64.22**	51.28
Natural gas liquids *($/bbl)*	**55.23**	43.11
Average liquids price	**62.21**	50.06
Natural gas *($/mcf)*	**10.17**	7.06
Total per boe *($/boe)*	**61.28**	44.69
Benchmark pricing		
Edmonton par - light oil *($/bbl)*	**69.33**	52.94
AECO-C Spot *($/mcf)*	**8.81**	6.59

Sales variance analysis

($000s)	Year ended December 31, 2005
Natural gas sales	
Volume increase	43,790
Price increase	22,588
Net gas sales change	66,378
Crude oil and NGL sales	
Volume increase	14,282
Price increase	4,403
Net crude oil and NGL sales change	18,685
Combined sales change	85,063

Revenues for the year ended December 31, 2005 increased 749 percent to $96,415 from $11,352 in the comparative period. The increase in revenue was a result of the 519 percent increase in production volumes and a 37 percent increase in the average sales price. The increase in the average sales price realized by Cyries is consistent with the increase in benchmark oil and natural gas prices. The average sales price for natural gas is at a premium to the AECO-C spot price due to the high energy content of the company's natural gas production.

The Company did not hedge or enter into any fixed price arrangements for the year ended December 31, 2005. As part of the Devlan acquisition the company acquired a fixed price crude oil collar to sell 200 boe/d of crude oil between $38.00 USD/bbl and $48.50 USD/bbl. The contract expired December 31, 2005. All the Company's remaining production is sold on the spot market. Therefore, both the historical prices received and future prices expected fluctuate with the prevailing market prices of crude oil and natural gas.

Royalties

Oil and natural gas royalties, net of the Alberta Royalty Tax Credit ("ARTC") increased to $23,749 for the year ended December 31, 2005 compared to $2,313 for the period ended December 31, 2004. The increase is due to the increase in petroleum and natural gas sales. The overall royalty rate of 25 percent of revenue increased from 20 percent for the period ended December 31, 2004. The higher royalty rates are the result of lower gas cost allowance recorded in 2005 and higher royalty rates associated with properties acquired in the third quarter of 2005. The Company expects the royalty rate to remain consistent in 2006. ARTC for the year ended December 31, 2005 increased to $114 from $39 for the period ended December 31, 2004.

Operating netback and production expense

($000s)	Year ended December 31, 2005	Period ended December 31, 2004
Revenue	**96,415**	11,352
Royalty income	**84**	5
	96,499	11,357
Royalties	**(23,749)**	(2,313)
Production expense (net)	**(11,989)**	(1,763)
Transportation expense	**(2,663)**	(414)
Operating netback	**58,098**	6,867
Operating netback per boe	**36.93**	27.04
Production expense gross	**13,563**	2,013
Overhead recoveries	**(1,075)**	(216)
Processing income	**(499)**	(34)
Production expense (net)	**11,989**	1,763
Production expense per boe (net)	**7.62**	6.94

Net production expenses increased for the year ended December 31, 2005 to $11,989 compared to $1,763 for the period ended December 31, 2004. The increase in production expense is due to the increased production and an increase in oil and natural gas production costs per barrel. Production costs per barrel increased 10 percent to $7.62 from $6.94 in the period ended December 31, 2004 for two reasons. Activity levels in Alberta have increased steadily over the past year resulting in higher demand for services and materials. This trend is expected to continue in the foreseeable future. Also, the operating costs per barrel for the assets acquired in the third quarter are higher than the historical operating costs of Cyries. It is anticipated that operating costs will remain at current levels for 2006.

The operating netback increased to $36.93 per boe from $27.04 per boe for the year ended December 31, 2004. The increase in the operating netback is due primarily to an increase in average sales price, offset slightly by an increase in operating and royalty expenses.

Transportation expense relates primarily to the cost of transporting natural gas on the main natural gas pipelines and a lesser amount for clean oil trucking charges. An increase in production volumes caused an increase in transportation costs to $2,663 for the year ended December 31, 2005 from $414 for the period ended December 31, 2004.

General and administrative expenses

($000s, except as indicated)	*Year ended December 31, 2005*	*Period ended December 31, 2004*
General and administrative expense (gross)	**4,278**	1,400
Overhead recoveries	**(1,276)**	(446)
General and administrative expense (net)	**3,002**	954
General and administrative *($/boe)*	**1.91**	3.75

General and administrative costs ("G&A") include costs incurred by the Company which are not directly associated with the production of oil and natural gas. For the year ended December 31, 2005, G&A was $3,002, compared to $954 for the period ended December 31, 2004. G&A has increased as the overall size of the business has grown; however, measured on a per barrel basis, the expense has decreased 49 percent to $1.91 per boe as a result of increased production volumes in 2005. G&A expense per barrel is expected to further decrease in 2006 as production volumes increase. The Company does not capitalize corporate general and administrative expenses.

Depreciation, depletion and accretion

Depletion, depreciation and accretion ("DD&A") increased to $23,840 for the year ended December 31, 2005 compared to $3,037 for the period ended December 31, 2004. The increase is due to higher average production in 2005 and an increase in DD&A per boe. DD&A expense per boe increased to $15.15 from $11.96 for the comparative period in 2004 as a result of increased finding and development costs associated with acquisitions and drilling in the current year. In determining the Company's depletion and depreciation, $18,715 (2004 - $4,216) of costs related to unproven properties and $13,375 (2004 - $3,661) of estimated salvage value was excluded from the costs subject to depletion. Future development costs required to complete wells for which proved reserves have been assigned of $10,600 (2004 - $2,083) were added to the Company's net book value in the depletion calculation.

Stock-based compensation

During 2005, stock-based compensation expense related to the outstanding stock options and Class B performance shares increased to $2,172 from $365 for the period ended December 31, 2004. The increase in stock compensation expense is due to the expense associated with the stock options issued in 2005. At December 31, 2005 there were 1,672 stock options outstanding compared to 460 at December 31, 2004.

Income taxes

For the year ended December 31, 2005 the Company recorded future income tax of $10,020 (2004 - 998) and current income taxes of $2,972 (2004 - nil) for an overall effective tax rate of 47 percent (2004 - 39 percent). In 2005 current tax expense includes a charge of $1,798 and future tax includes an expense of $30 arising from an income tax audit performed on certain Devlan Exploration Inc. filings. Estimated interest of $607 is included in interest expense. The additional income tax increased the effective tax rate by six percent. The remaining current tax expense is due to capital taxes of $252 and income taxes of $922 of a subsidiary. The Company does not expect significant income taxes in 2006 based on current oil and natural gas prices and the planned capital expenditures for 2006. Income taxes for the Company's stand-alone subsidiary are estimated to be $1,000 for 2006.

The estimated consolidated tax pools at December 31, 2005 are included in the table below.

($000s)	***Year ended December 31, 2005***
Canadian exploration expense	12,210
Canadian development expense	44,825
Canadian oil and gas property expense	46,428
Foreign exploration and development expense	632
Undepreciated capital cost	44,403
Share issue costs	5,601

On March 2, 2005, Devlan issued flow-through shares and committed to spend $2,250 before December 31, 2005 on expenditures qualifying as Canadian exploration expenditures. Flow-through expenditures on Canadian exploration expenses were renounced to subscribers of the flow-through common shares in February 2006 effective December 31, 2005. The related income tax impact has been recorded in the first quarter of 2006.

Capital expenditures

($000s)	***Year ended December 31, 2005***	***Period ended December 31, 2004***
Corporate acquisitions	**125,229**	-
Land acquisitions	**12,173**	1,867
Property acquisitions (net)	**346**	4,993
Geological and geophysical	**4,946**	1,565
Drilling and completions	**68,827**	20,271
Equipment and facilities	**15,220**	3,835
Other	**79**	27
Total capital expenditures	**226,820**	32,558

For the year ended December 31, 2005, Cyries' capital expenditure program was focused on drilling natural gas prospects in the Deep Basin and Peace River Arch. The Company drilled 64.0 gross wells (42.9 net) with an 80 percent success rate. Of the total wells drilled, 41.0 (29.1 net) were natural gas wells and 11.0 (5.0 net) were oil wells. Facility expenditures for the year relate primarily to two additional compressor stations and the costs associated with connecting successful wells to existing infrastructure and processing facilities.

Corporate acquisitions of $125,229 include the fair value of the property, plant and equipment acquired through acquisition. The fair value assigned to the property, plant and equipment for the Devlan and 1181608 Alberta ULC acquisitions was $70,512 and $54,717, respectively.

	Year ended December 31, 2005		Period ended December 31, 2004	
	Gross wells	Net wells	Gross wells	Net wells
Gas	**41.0**	**29.1**	9.0	6.5
Oil	**11.0**	**5.0**	8.0	6.4
Dry	**12.0**	**8.8**	-	-
Total	**64.0**	**42.9**	17.0	12.9
Success *(%)*		**80%**		100%

Share capital

(000s)	
Weighted average common shares outstanding at December 31, 2005	
Basic	32,286
Diluted	36,416
Outstanding securities at March 15, 2006	
Common shares	39,265
Warrants	3,968
Performance shares	599
Stock options	1,677
Total outstanding securities at March 15, 2006	45,509

Equity issues

	Date of issue	Price per share of issue	Shares issued	Gross proceeds
Common shares	June 28, 2004	$ 1.27	3,988	$ 5,065
Common shares	July 28, 2004	5.50	4,000	22,000
Common shares	February 3, 2005	8.20	2,440	20,008
Common shares	July 1, 2005	9.52	8,558	81,469
Common shares	August 12, 2005	$ 12.45	4,017	50,005
Total			23,003	$ 178,547

On June 28, 2004 the Company issued 3,988 common shares and 3,988 warrants in an initial private placement of its common shares at a price of $1.63 per common share. Both the shares and warrants are subject to vesting provisions. One third of the common shares purchased in the private placement became eligible for resale on each of December 31, 2004 and June 28, 2005 with the remaining one third becoming eligible on June 28, 2006.

Each warrant is exercisable into one common share of the Company at a price of $1.63 per share until the warrants expire on June 28, 2008. One third of the warrants vest annually subject to certain performance clauses, with the initial tranche vesting June 28, 2005. The initial one third of the warrants vested on the first anniversary date as the Cyries common shares traded at a 20-day weighted average price of at least $2.45.

For the remaining two-thirds of the warrants to vest on their respective anniversary dates the Cyries common shares must, at any time during the term of the warrants, trade at a 20-day weighted average price of at least $3.26. The performance clauses have been met as of December 31, 2005.

In conjunction with the initial private placement, 605 performance shares were issued to employees and directors for consideration of $0.01 per share. The performance shares vest equally over three years and are convertible into the fraction of a common share equal to the closing trading price of the common shares on the Toronto Stock Exchange on the day prior to such conversion less $1.63, if positive, divided by the common share closing price.

During the year, the company issued 1,222 stock options to employees and directors. The options vest over four years and are exercisable into common shares at an average price of $12.03. At December 31, 2005 the Company had 1,672 options outstanding with an average exercise price of $10.25.

During the year, the Company raised a total of $151 million through equity issues, share purchases and private placements; $20 million of equity issues allowed for the 2005 capital budget to be increased and; $131 million funded the acquisitions of Devlan and 1181608 Alberta ULC.

Liquidity and capital resources

At December 31, 2005 the Company had bank debt of $47,249 and a working capital deficiency of $25,971. The Company's bank lines are limited to $73 million. The Company's bank line is subject to semi-annual review with the next review occurring in April 2006.

The 2006 capital program is anticipated to be $130 million and will be funded through a combination of cash flow from operations and bank debt. The growth in production and higher commodity prices has increased the Company's ability to fund the capital program with internally generated funds. However, fluctuations in crude oil and natural gas prices will have a large impact on the Company's capital program and working capital position. The Company will monitor the capital program with the current price outlook and adjust it accordingly.

Commodity prices and production volumes have the largest impact on the ability for Cyries to generate adequate cash flow to meet all its obligations. A prolonged decrease in commodity prices would negatively affect cash flow from operations and would also likely result in a reduction in the amount of bank loan available. If the capital expenditure program does not result in sufficient additional reserves and/or production it would likely have a negative impact on the Company's ability to carry out its planned capital program.

Cyries may adjust its capital expenditure program depending on the commodity price outlook. The Company believes that internally generated cash flow and incremental bank debt should be sufficient to finance current operations and planned capital spending in the next year.

Quarterly financial and operational information

($000s, except as indicated)	**Q4 2005**	Q3 2005	Q2 2005	Q1 2005	Q4 2004	Q3 2004
Average production *(boe/d)*	**6,522**	5,525	2,768	2,368	1,644	1,142
Average sales price *($/boe)*	**70.69**	61.26	50.77	47.24	45.19	43.95
Petroleum and natural gas sales	**42,419**	31,140	12,787	10,069	6,834	4,518
Royalties	**11,394**	7,125	2,882	2,348	1,226	1,086
Operating expenses	**4,804**	3,992	1,755	1,438	1,075	688
General and administrative expenses	**1,115**	648	777	462	519	435
Cash flow from operations	**20,861**	17,650	6,857	5,496	3,783	2,167
Per share basic *($)*	**0.53**	0.47	0.26	0.21	0.16	0.09
Per share diluted *($)*	**0.48**	0.42	0.22	0.19	0.14	0.08
Net earnings	**5,682**	6,101	1,822	1,227	1,171	379
Per share basic *($)*	**0.14**	0.16	0.07	0.05	0.05	0.02
Per share diluted *($)*	**0.13**	0.15	0.06	0.04	0.04	0.01
Total assets	**364,230**	326,177	100,490	94,901	69,711	59,537
Bank debt and working capital deficiency (excess)	**73,220**	56,238	18,322	10,654	9,313	(3,581)

Production

Production during the fourth quarter of 2005 increased 18 percent to 6,522 boe per day compared with 5,525 boe per day in the prior quarter. The production increase is primarily due to successful drilling in the Deep Basin/Peace River Arch area in fourth quarter of 2005. Production increased by 297 percent from the 1,644 boe per day recorded in the fourth quarter of 2004 due to the acquisitions in 2005 coupled with a successful capital program.

Petroleum and natural gas sales

Oil and natural gas revenues increased 36 percent in the fourth quarter of 2005 compared to the third quarter 2005 as production volumes increased and the average oil and natural gas price increased by 15 percent. Quarterly petroleum and natural gas sales and net earnings have increased over the past six quarters beginning July 2, 2004 due to increased production resulting from a successful drilling program, increased oil and natural gas prices and two corporate acquisitions.

Royalties

Royalties, net of ARTC, increased 60 percent to $11,394 when compared to the third quarter of 2005. As a percentage of sales, royalty rates increased from 23 percent in third quarter to 27 percent in the fourth quarter of 2005. The increase in average royalty rate is due to a reduction in ARTC and an increase in gross overriding royalties in the quarter.

Compared to the fourth quarter of 2004, royalties increased 829 percent in the fourth quarter of 2005. The royalty rate increased from 18 percent to 27 percent due to a reduction in the gas cost allowance in 2005 and higher royalty rates associated with properties acquired in 2005.

Operating expenses

The increase in production volumes and higher than expected third party processing fees increased fourth quarter 2005 operating expenses by 347 percent and 20 percent when respectively compared to fourth quarter 2004 and third quarter of 2005. On a per boe basis, operating expenses increased slightly to $8.01 compared to $7.85 per boe in the previous quarter.

General and administrative expenses

G&A increased 72 percent when compared to the prior quarter and 115 percent when compared to fourth quarter 2004. The increases in G&A are due to the overall increase in the size of the business. G&A was $1.86 per boe in the fourth quarter of 2005 increasing from $1.27 per boe in the third quarter of 2005 and decreasing from $3.43 per boe in the fourth quarter of 2004. The decrease from prior year is due to increased production volumes in 2005.

Net earnings and cash flow from operations

Overall, the increase in production and stable oil and natural gas prices resulted in an increase in net earnings and cash flow from operations for the fourth quarter of 2005. Cash flow has increased throughout the last six quarters, increasing 451 percent to $20,861 ($0.53 per basic share) in the fourth quarter of 2005 from the comparable quarter in 2004 and increasing 18 percent from the prior quarter. Net earnings for the fourth quarter of 2005 increased to $5,682 ($0.14 per basic share) from $1,171 ($0.05 per basic share) recorded in the comparable period in 2004. Net earnings in the fourth quarter of 2005 decreased 7 percent from $6,101 ($0.16 per basic share) recorded in the prior quarter. An income tax audit in the period resulted in an increase in current tax expense of $1,798 and related interest of $607. This increase offset the positive increases from higher average production and sales price in the quarter.

Total assets

Total assets increased 12 percent to $364,230 at the end of the fourth quarter of 2005 compared to the prior quarter. The increase is attributable to an increase in drilling and capital spending in the fourth quarter of 2005. The 423 percent increase in total assets from December 31, 2004 is primarily due to capital expenditures of $101,591 and acquisitions of $125,229 in 2005. The capital expenditures in fourth quarter of 2005 included $5,049 land acquisitions, $581 of net property acquisitions, $1,908 of geological and geophysical activities, $25,094 in drilling and completions and $5,164 in equipment and facilities.

Working capital deficiency

The bank and working capital deficiency has increased throughout 2005 as a result of using leverage to fund a portion the corporation's drilling and acquisition program and assuming approximately $22,500 in debt in the Devlan acquisition.

Controls and procedures

The preparation of the MD&A is supported by a set of disclosure controls and procedures under management's responsibility. For the 2005 year-end, this control structure was reviewed and the effectiveness of its design and operation was evaluated.

The evaluation confirmed the effectiveness of the design and operations of disclosure controls and procedures as at December 31, 2005. The evaluation was conducted in accordance with the requirements of Multilateral Instrument 52-109 of the Canadian Securities Administrators.

CRITICAL ACCOUNTING ESTIMATES

Oil and gas reserves

Full cost accounting depends on the estimated proven reserves which the Company believes to be recoverable from oil and gas properties by applying significant judgments relating to available geological, geophysical, engineering and economic data. Estimates are reviewed and revised as appropriate. Changes in estimates can occur as a result of changes in the economic conditions impacting oil and gas prices and costs as well as additional information becoming available from production performance and development activities.

Depletion and depreciation

The company uses the full cost method of accounting for exploration and development activities whereby all of the costs associated with these activities are capitalized, whether successful or not. The aggregate of capitalized costs, net of certain costs related to unproved properties, and estimated future development costs is amortized using the unit-of-production method based on estimated proved reserves. Changes in estimated proved reserves or future development costs have a direct impact on depletion and depreciation expense. Certain costs related to unproved properties and major development projects may be excluded from costs subject to depletion until proved reserves have been determined or their value is impaired. These properties are reviewed quarterly to determine if proved reserves should be assigned, at which point they would be included in the depletion calculation, or for impairment, for which any write-down would be charged to depletion and depreciation.

Full cost accounting ceiling test

Oil and gas assets are evaluated at least annually to determine that the costs are recoverable and do not exceed the fair value of the properties. The costs are assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves and the lower of cost and market of unproved properties exceed the carrying value of the oil and gas assets. If the carrying value of the oil and gas assets is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted future cash flows from the production of proved and probable reserves and the lower of cost and market of the unproved properties. The cash flows are estimated using the future product prices and costs and are discounted using the risk-free rate. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material. Any impairment would be charged as additional depletion and depreciation expense.

Goodwill

Goodwill represents the excess of the purchase price of Devlan and 1181608 Alberta ULC over the fair value of net assets acquired. Goodwill is assessed for impairment at least annually. If it is determined that the fair value of the assets and liabilities is less than the book value at the time of assessment, an impairment amount is determined by deducting the fair value from the book value and applying it against the book value of goodwill. Any excess of the book value of goodwill over the implied fair value is the impairment amount and will be charged to income in the period of the impairment.

Asset retirement obligations

The Company records a liability for the fair value of legal obligations associated with the retirement of long-lived tangible assets in the period in which they are incurred, normally when the asset is purchased or developed. On recognition of the liability there is a corresponding increase in the carrying amount of the related asset and the asset retirement obligation. The total amount of the asset retirement obligation is an estimate based on the Company's net ownership interest in all wells and facilities, the estimated costs to abandon and reclaim the wells and facilities and the estimated timing of the costs to be incurred in future periods. The total amount of the estimated cash flows required to settle the asset retirement obligation, the timing of those cash flows and the discount rate used to calculate the present value of those cash flows are estimates subject to measurement uncertainty. Any change in these estimates would impact the asset retirement liability.

Stock-based compensation

The Company accounts for stock options using the fair value method whereby stock-based compensation expense is recorded for all options granted with a corresponding increase recorded to contributed surplus. The fair value of the options granted are estimated at the date of grant using the Black-Scholes valuation model. Upon exercise of the stock options, consideration paid by employees or directors together with the amount previously recognized in contributed surplus is recorded as an increase to share capital.

Income taxes

The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from the liability estimated or recorded.

Other estimates

The accrual method of accounting requires management to incorporate certain estimates including estimates of revenues, royalties and production costs as at a specific reporting date but for which actual revenues and costs have not yet been received; and estimates on capital projects which are in progress or recently completed where actual costs have not been received at a specific reporting date.

The Company ensures that the individuals with the most knowledge of the activity are responsible for the estimate. These estimates are then reviewed for reasonableness and past estimates are compared to actual results in order to make informed decisions on future estimates.

RISKS AND UNCERTAINTIES

Exploration, development and production risks

Oil and natural gas exploration involves a high degree of risk, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. There is no assurance that expenditures made on future exploration by Cyries will result in new discoveries of oil or natural gas in commercial quantities.

It is difficult to project the costs of implementing an exploratory drilling program due to the inherent uncertainties of drilling in unknown formations, the costs associated with encountering various drilling conditions such as over pressured zones and tools lost in the hole, and changes in drilling plans and locations as a result of prior exploratory wells or additional seismic data and interpretations thereof.

The long-term commercial success of Cyries depends on its ability to find, acquire, develop and commercially produce oil and natural gas reserves. No assurance can be given that Cyries will be able to continue to locate satisfactory properties for acquisition or participation. Moreover, if such acquisitions or participations are identified, Cyries may determine that current markets, terms of acquisition and participation or pricing conditions make such acquisitions or participations uneconomic.

Future oil and gas exploration may involve unprofitable efforts, not only from dry wells, but from wells that are productive but do not produce sufficient net revenues to return a profit after drilling, operating and other costs. Completion of a well does not assure a profit on the investment or recovery of drilling, completion and operating costs. In addition, drilling hazards or environmental damage could greatly increase the cost of operations, and various field operating conditions may adversely affect the production from successful wells. These conditions include delays in obtaining governmental approvals or consents, shut-ins of connected wells resulting from extreme weather conditions, insufficient storage or transportation capacity or other geological and mechanical conditions. While diligent well supervision and effective maintenance operations can contribute to maximizing production rates over time, production delays and declines from normal field operating conditions cannot be eliminated and can be expected to adversely affect revenue and cash flow levels to varying degrees.

In addition, oil and gas operations are subject to the risks of exploration, development and production of oil and natural gas properties, including encountering unexpected formations or pressures, premature declines of reservoirs, blow-outs, cratering, sour gas releases, fires and spills. Losses resulting from the occurrence of any of these risks could have a materially adverse effect on future results of operations, liquidity and financial condition.

Prices, markets and marketing of crude oil and natural gas

Oil and natural gas are commodities whose prices are determined based on world demand, supply and other factors, all of which are beyond the control of Cyries. World prices for oil and natural gas have fluctuated widely in recent years. Any material decline in prices could result in a reduction of net production revenue. Certain wells or other projects may become uneconomic as a result of a decline in world oil prices and natural gas prices, leading to a reduction in the volume of Cyries' oil and gas reserves. Cyries might also elect not to produce from certain wells at lower prices. All of these factors could result in a material decrease in Cyries' future net production revenue, causing a reduction in its oil and gas acquisition and development activities. In addition, bank borrowings available to Cyries are in part determined by the borrowing base of Cyries. A sustained material decline in prices from historical average prices could limit Cyries' borrowing base, therefore reducing the bank credit available to Cyries, and could require that a portion of any existing bank debt of Cyries be repaid.

In addition to establishing markets for its oil and natural gas, Cyries must also successfully market its oil and natural gas to prospective buyers. The marketability and price of oil and natural gas, which may be acquired or discovered by Cyries, will be affected by numerous factors beyond its control. Cyries will be affected by the differential between the price paid by refiners for light quality oil and the grades of oil produced by Cyries. The ability of Cyries to market its natural gas may depend upon its ability to acquire space on pipelines which deliver natural gas to commercial markets. Cyries will also likely be affected by deliverability uncertainties related to the proximity of its reserves to pipelines and processing facilities and related to operational problems with such pipelines and facilities and extensive government regulation relating to price, taxes, royalties, land tenure, allowable production, the export of oil and natural gas and many other aspects of the oil and natural gas business. Cyries has limited direct experience in the marketing of oil and natural gas.

Substantial capital requirements; liquidity

Cyries anticipates that it will make substantial capital expenditures for the acquisition, exploration, development and production of oil and natural gas reserves in the future. If Cyries' revenues or reserves decline, Cyries may have limited ability to expend the capital necessary to undertake or complete future drilling programs. There can be no assurance that debt or equity financing, or cash generated by operations will be available or sufficient to meet these requirements or for other corporate purposes or, if debt or equity financing is available, that it will be on terms acceptable to Cyries. Moreover, future activities may require Cyries to alter its capitalization significantly. The inability of Cyries to access sufficient capital for its operations could have a material adverse effect on Cyries' financial condition, results of operations or prospects.

Cyries' lenders have been provided with security over substantially all of the assets of Cyries. If Cyries becomes unable to pay its debt service charges or otherwise commits an event of default, such as bankruptcy, these lenders may foreclose on or sell Cyries' properties. The proceeds of any such sale would be applied to satisfy amounts owed to Cyries' lenders and other creditors and only the remainder, if any, would be available to Cyries.

Competition

Cyries actively competes for reserve acquisitions, exploration leases, licences and concessions and skilled industry personnel with a substantial number of other oil and gas companies, many of which have significantly greater financial resources than Cyries. Cyries' competitors include major integrated oil and natural gas companies and numerous other independent oil and natural gas companies and individual producers and operators.

The oil and gas industry is highly competitive. Cyries' competitors for the acquisition, exploration, production and development of oil and natural gas properties, and for capital to finance such activities, include companies that have greater financial and personnel resources available to them than Cyries.

Certain of Cyries' customers and potential customers are themselves exploring for oil and natural gas, and the results of such exploration efforts could affect Cyries' ability to sell or supply oil or gas to these customers in the future. Cyries' ability to successfully bid on and acquire additional property rights, to discover reserves, to participate in drilling opportunities and to identify and enter into commercial arrangements with customers will be dependent upon developing and maintaining close working relationships with its future industry partners and joint operators and its ability to select and evaluate suitable properties and to consummate transactions in a highly competitive environment.

Environmental risks

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions and state and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. No assurance can be given that environmental laws will not result in a curtailment of production or a material increase in the costs of production, development or exploration activities or otherwise adversely affect Cyries' financial condition, results of operations or prospects.

Insurance

Cyries' involvement in the exploration for and development of oil and gas properties may result in Cyries becoming subject to liability for pollution, blow-outs, property damage, personal injury or other hazards. Although Cyries has obtained insurance in accordance with industry standards to address such risks, such insurance has limitations on liability that may not be sufficient to cover the full extent of such liabilities. In addition, such risks may not, in all circumstances be insurable or, in certain circumstances, Cyries may elect not to obtain insurance to deal with specific risks due to the high premiums associated with such insurance or other reasons. The payment of such uninsured liabilities would reduce the funds available to Cyries. The occurrence of a significant event that Cyries is not fully insured against, or the insolvency of the insurer of such event, could have a material adverse effect on Cyries' financial position, results of operations or prospects.

Kyoto Protocol

Canada is a signatory to the United Nations Framework Convention on Climate Change. Canada has ratified the Kyoto Protocol established thereunder. Annex B parties to the Kyoto Protocol, which includes Canada, are required to establish legally binding targets to reduce nation-wide emissions of carbon dioxide, methane, nitrous oxide and other so-called "greenhouse gases". Cyries' exploration and production facilities and other operations and activities emit a small amount of greenhouse gasses which may subject Cyries to legislation in Canada regulating emissions of greenhouse gases. The Government of Canada has put forward a Climate Change Plan for Canada which suggests further legislation to set greenhouse gases emission reduction requirements for various industrial activities, including oil and gas exploration and production. Future Canadian federal legislation, together with provincial emission reduction requirements, such as those proposed in the Climate Change and Emissions Management Act (Alberta), may require the reduction of emissions or emissions intensity from Cyries' operations and facilities. The direct and indirect costs of complying with these emissions regulations may adversely affect the business of Cyries.

Reserve replacement

Cyries' future oil and natural gas reserves, production, and cash flows to be derived therefrom are highly dependent on Cyries successfully acquiring or discovering new reserves. Without the continual addition of new reserves, any existing reserves Cyries may have at any particular time and the production there from will decline over time as such existing reserves are exploited. A future increase in Cyries' reserves will depend not only on Cyries' ability to develop any properties it may have from time to time, but also on its ability to select and acquire suitable producing properties or prospects. There can be no assurance that Cyries' future exploration and development efforts will result in the discovery and development of additional commercial accumulations of oil and natural gas.

Reliance on operators and key employees

To the extent Cyries is not the operator of its oil and gas properties, Cyries will be dependent on such operators for the timing of activities related to such properties and will largely be unable to direct or control the activities of the operators. In addition, the success of Cyries will be largely dependent upon the performance of its management and key employees. Cyries does not have any key man insurance policies, and therefore there is a risk that the death or departure of any member of management or any key employee could have a material adverse effect on Cyries.

Corporate matters

To date, Cyries has not paid any dividends on the Cyries Shares and does not anticipate the payment of any dividends on the Cyries Shares for the foreseeable future. Certain of the directors and officers of Cyries are also directors and officers of other oil and gas companies involved in natural resource exploration and development, and conflicts of interest may arise between their duties as officers and directors of Cyries and as officers and directors of such other companies. Such conflicts must be disclosed in accordance with, and are subject to such other procedures and remedies as applicable under the ABCA.

Additional funding requirements

Cyries' cash flow from its reserves may not be sufficient to fund its ongoing activities at all times. From time to time, Cyries may require additional financing in order to carry out its oil and gas acquisition, exploration and development activities. Failure to obtain such financing on a timely basis could cause Cyries to forfeit its interest in certain properties, miss certain acquisition opportunities and reduce or terminate its operations. If Cyries' revenues from its reserves decrease as a result of lower oil and natural gas prices or otherwise, it will affect Cyries' ability to expend the necessary capital to replace its reserves or to maintain its production. If Cyries' cash flow from operations is not sufficient to satisfy its capital expenditure requirements, there can be no assurance that additional debt or equity financing will be available to meet these requirements or available on terms acceptable to Cyries.

From time to time Cyries may enter into transactions to acquire assets or the shares of other corporations. These transactions may be financed partially or wholly with debt, which may increase Cyries' debt levels above industry standards. Neither Cyries' articles nor its by-laws limit the amount of indebtedness that Cyries may incur. The level of Cyries' indebtedness from time to time could impair Cyries' ability to obtain additional financing in the future on a timely basis to take advantage of business opportunities that may arise.

Title to properties

Although title reviews will be done according to industry standards prior to the purchase of most oil and natural gas producing properties or the commencement of drilling wells, such reviews do not guarantee or certify that an unforeseen defect in the chain of title will not arise to defeat the claim of the Corporation which could result in a reduction of the revenue received by the Corporation.

Delays in business operations

In addition to the usual delays in payments by purchasers of oil and natural gas to Cyries or to the operators, and the delays by operators in remitting payment to Cyries, payments between these parties may be delayed due to restrictions imposed by lenders, accounting delays, delays in the sale or delivery of products, delays in the connection of wells to a gathering system, adjustment for prior periods, or recovery by the operator of expenses incurred in the operation of the properties. Any of these delays could reduce the amount of cash flow available for the business of Cyries in a given period and expose Cyries to additional third party credit risks. The level of activity in the Canadian oil and gas industry is influenced by seasonal weather patterns. Wet weather and spring thaw may make the ground unstable. Consequently, municipalities and provincial transportation departments enforce road bans that restrict the movement of rigs and other heavy equipment, thereby reducing activity levels. Also, certain oil and gas producing areas are located in areas that are inaccessible other than during the winter months because the ground surrounding the sites in these areas consists of swampy terrain. Seasonal factors and unexpected weather patterns may lead to declines in exploration and production activity and corresponding declines in the demand for the goods and services of Cyries.

Changes in legislation

The return on an investment in securities of Cyries is subject to changes in Canadian federal and provincial tax laws and government incentive programs and there can be no assurance that such laws or programs will not be changed in a manner that adversely affects Cyries or the holding and disposing of the securities of Cyries.

Income taxes

The Corporation has filed or will file all required income tax returns and believes that it is in full compliance with the provisions of the Income Tax Act (Canada) and all applicable provincial tax legislation. However, such returns are subject to reassessment by the applicable taxation authority. In the event of a successful reassessment of the Corporation, whether by re-characterization of exploration and development expenditures or otherwise, such reassessment may have an impact on current and future taxes payable.

Assessments of value of acquisitions

Acquisitions of oil and gas issuers and oil and gas assets are typically based on engineering and economic assessments made by independent engineers and Cyries' own assessments. These assessments both will include a series of assumptions regarding such factors as recoverability and marketability of oil and gas, future prices of oil and gas and operating costs, future capital expenditures and royalties and other government levies which will be imposed over the producing life of the reserves. Many of these factors are subject to change and are beyond Cyries' control. In particular, the prices of and markets for oil and natural gas products may change from those anticipated at the time of making such assessment.

In addition, all such assessments involve a measure of geologic and engineering uncertainty which could result in lower production and reserves than anticipated. Initial assessments of acquisitions may be based on reports by a firm of independent engineers that are not the same as the firm that Cyries uses for its year end reserve evaluations.

Third party credit risk

Cyries is or may be exposed to third party credit risk through its contractual arrangements with its current or future joint venture partners, marketers of its petroleum and natural gas production and other parties. In the event such entities fail to meet their contractual obligations to Cyries, such failures could have a material adverse effect on Cyries and its cash flow from operations.

Management, in accordance with Canadian generally accepted accounting principles, has prepared the accompanying financial statements of Cyries Energy Inc. Financial and operating information presented throughout this Annual Report is consistent with that shown in the financial statements.

Management is responsible for the integrity of the financial information. Internal control systems are designed and maintained to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for financial reporting purposes.

The Board of Directors is responsible for ensuring management fulfills its responsibilities for financial reporting and internal controls. The Board exercises this responsibility with the assistance of the Audit Committee. The Committee meets with management and the independent auditors to ensure that management's responsibilities are properly discharged, to review the financial statements before they are presented to the Board for approval.

The shareholders have appointed Deloitte and Touche LLP as the external auditors of the Company and, in that capacity, they have examined the financial statements for the year ended December 31, 2005. The Auditor's Report to the shareholders is presented herein.

Donald F. Archibald
Chairman and Chief Executive Officer
March 9, 2006

Erin Thorson
Chief Financial Officer and Controller

AUDITORS' REPORT

To the Shareholders of Cyries Energy Inc.:

We have audited the consolidated balance sheet of Cyries Energy Inc. (the "Company") as at December 31, 2005 and 2004 and the consolidated statement of earnings and retained earnings and cash flows for the year ended December 31, 2005 and the period July 2, 2004 to December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the year ended December 31, 2005 and the period July 2, 2004 to December 31, 2004 in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Calgary, Alberta
March 9, 2006

($000s)	As at December 31, 2005	December 31, 2004
Assets		
Current assets		
Accounts receivable	**28,948**	8,916
Deposits and prepaid expenses	**1,835**	606
	30,783	9,522
Future income tax asset *(note 6)*	**-**	3,267
Property and equipment, net *(note 5)*	**265,013**	56,922
Goodwill *(note 4)*	**68,434**	-
	364,230	69,711
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable and accrued liabilities	**53,343**	15,743
Income taxes payable *(note 6)*	**3,411**	-
Revolving demand loan *(note 7)*	**47,249**	3,092
	104,003	18,835
Future income tax liability *(note 6)*	**33,158**	-
Asset retirement obligations *(note 11)*	**12,440**	2,519
Total liabilities	**149,601**	21,354
Shareholders' equity		
Share capital *(note 8)*	**195,734**	46,441
Contributed surplus *(note 9)*	**2,512**	365
Retained earnings	**16,383**	1,551
	214,629	48,357
	364,230	69,711

See accompanying notes.

On behalf of the Board:

Donald F. Archibald
Chairman, CEO & Director

Douglas A. Dafoe
Director

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS

($000s, except per share amounts)	**Year ended December 31, 2005**	**For the period July 2, 2004 to December 31, 2004** *(note 1)*
Revenue		
Petroleum and natural gas sales	**96,415**	11,352
Royalties (net of Alberta Royalty Tax Credit)	**(23,749)**	(2,313)
	72,666	9,039
Other income	**131**	70
	72,797	9,109
Expenses		
Production	**11,989**	1,763
Transportation	**2,663**	414
General and administrative	**3,002**	954
Interest	**1,307**	27
Stock compensation	**2,172**	365
Depletion, depreciation and accretion	**23,840**	3,037
	44,973	6,560
Earnings before taxes	**27,824**	2,549
Taxes *(note 6)*		
Current income taxes	**2,972**	-
Future income taxes	**10,020**	998
Net earnings	**14,832**	1,551
Retained earnings, beginning of period	**1,551**	-
Retained earnings, end of period	**16,383**	1,551
Net earnings per share *(note 10)*		
Basic	**$0.46**	$0.07
Diluted	**$0.41**	$0.06
Weighted average common shares outstanding		
Basic	**32,286**	23,646
Diluted	**36,416**	27,082

See accompanying notes.

($000s, except per share amounts)	Year ended December 31, 2005	For the period July 2, 2004 to December 31, 2004 (note 1)
Operating activities		
Net earnings for the period	**14,832**	1,551
Items not affecting cash		
Depletion, depreciation and accretion	**23,840**	3,037
Future income taxes	**10,020**	998
Stock compensation	**2,172**	365
Cash flow from operations, before non-cash working capital changes	**50,864**	5,951
Net changes in non-cash operating working capital *(note 12)*	**2,197**	(2,574)
	53,061	3,376
Financing activities		
Issue of common shares	**70,013**	28,506
Issue of common shares on exercise of options and warrants	**86**	-
Share issue costs	**(3,528)**	(1,211)
Increase/(decrease) in bank debt	**24,949**	(6,908)
	91,520	20,387
Investing activities		
Additions to property and equipment	**(108,400)**	(32,558)
Corporate acquisitions	**(57,466)**	-
Disposition of property and equipment	**6,810**	-
Net changes in non-cash investing working capital *(note 12)*	**14,475**	8,795
	(144,581)	(23,763)
Change in cash	**-**	-
Cash, beginning of period	**-**	-
Cash, end of period	**-**	-

See accompanying notes.

1. NATURE OF BUSINESS

Cyries Energy Inc. ("Cyries" or the "Company") was incorporated May 20, 2004 and commenced operations on July 2, 2004 when certain assets of Cequel Energy Ltd. ("Cequel") were transferred to Cyries under a Plan of Arrangement entered into by Progress Energy Ltd. ("Progress"), Cequel, Progress Energy Trust, Cyries and ProEx Energy Ltd. (the "Arrangement"). Cyries is engaged in the exploration, development and production of crude oil and natural gas in the province of Alberta.

2. SIGNIFICANT ACCOUNTING POLICIES

a) Basis of presentation

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles within the framework of accounting policies summarized below.

b) Revenue recognition

Revenues associated with sales of petroleum and natural gas and all other items are recorded when title passes to the customer. Revenues are recorded gross of transportation charges incurred by the Company.

c) Property and equipment

Capitalized costs
The Company follows the full cost method of accounting whereby all costs relating to the exploration for and development of petroleum and natural gas reserves, whether productive or unproductive, are capitalized in one Canadian cost center and are charged against earnings, as set out below. Such costs include land and lease acquisitions, geological and geophysical expenditures, drilling of productive and non-productive wells, production and gathering equipment and facilities, carrying costs directly related to unproved properties and corporate expenses directly related to acquisition, exploration and development activities. Proceeds from the disposition of petroleum and natural gas properties are accounted for as a reduction of capitalized costs, with no gain or loss recognized unless such disposition results in a change of 20 percent or more in the depletion and depreciation rate.

Depletion and depreciation
Depletion and depreciation of petroleum and natural gas properties and equipment are calculated using a unit of production method based on estimated gross proved petroleum and natural gas reserves, as determined by independent engineers. For purposes of this calculation, petroleum and natural gas reserves are converted to a common unit of measurement on the basis of six thousand cubic feet of gas equates to one barrel of oil. In determining its depletion base, the Company includes estimated future costs to be incurred in developing proved reserves and excludes estimated salvage values and the cost of unproved properties. Costs of acquiring and evaluating unproved properties are excluded from the depletion base until it is determined whether proved reserves are attributable to the properties or impairment occurs. Unproved properties are assessed for impairment at least annually.

Ceiling test
Impairment is determined when the carrying amount of the property, plant and equipment exceeds the sum of the undiscounted cash flows expected to result from the Company's proved reserves. If the carrying value is impaired, the amount of impairment is measured by comparing the carrying amounts of the property, plant and equipment to an amount equal to the estimated net present value of future cash flows from proved plus probable reserves. This calculation incorporates risks and uncertainties in the expected future cash flows that are discounted using a risk-free rate. Any excess carrying value above the net present value of the future cash flows would be recorded as a permanent impairment and charged to earnings.

d) Joint interests

A portion of the Company's exploration, development and production activities is conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

e) Measurement uncertainty

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingencies. Such estimates primarily relate to unsettled transactions and events at the balance sheet date. Actual results could differ from those estimated.

The amounts recorded for depreciation and depletion of petroleum and natural gas property and equipment and for asset retirement obligations are based on estimates of petroleum and natural gas reserves and future costs. Proved reserves also provide the basis for determining whether the carrying value of property, plant and equipment is impaired. The determination of stock compensation involves estimates of the volatility of the Company's common shares, forfeiture rates and expected life. By their nature, these estimates are subject to measurement uncertainty, and the impact on the financial statements of future periods could be material.

f) Stock based compensation

The Company accounts for its stock based compensation plans using the fair value method. Fair value is determined at the grant date using the Black-Scholes option-pricing model and is recognized over the vesting period of the options and performance shares granted as stock compensation expense and contributed surplus. The contributed surplus balance is reduced as the options and performance shares are exercised and the amount initially recorded is credited to share capital.

g) Future income taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income tax is based on the differences between assets and liabilities reported for financial reporting purposes and those reported for income tax purposes. Future income taxes are measured using enacted tax rates and laws that will be in effect when the differences are expected to reverse. The effect on future tax assets and liabilities of a change in tax rates is recognized in net earnings in the period in which the change occurs. Future income tax assets are limited to the amount that is more likely than not to be realized.

h) Earnings per share

Basic earnings per share is computed by dividing net earnings by the weighted average number of common shares outstanding during the period. The treasury stock method is used to determine the dilutive effect of stock options, performance shares and warrants, whereby proceeds from the exercise of in-the-money stock options or other dilutive instruments would be used to purchase common shares at the average market price during the period.

i) Asset retirement obligations

The Company recognizes the estimated liability associated with an asset retirement obligation ("ARO") in the financial statements at the time the asset is acquired and the liability is incurred. The estimated fair value of the ARO liability is recorded as a long term liability, with a corresponding increase in the carrying amount of property, plant and equipment. The capitalized amount is depleted on a unit-of-production method over the life of the proved reserves. The liability amount is increased each reporting period due to the passage of time and the amount of accretion is charged to earnings in the period. The ARO can also increase or decrease due to changes in the estimates of timing of cash flows or changes in

the original estimated undiscounted cost. Actual costs incurred upon settlement of the ARO are charged against the ARO to the extent of the liability recorded.

j) Goodwill

Goodwill is the residual amount that results when the purchase price of a business exceeds the fair value of the net identifiable assets and liabilities. Goodwill is stated at cost and is not amortized. The goodwill balance is assessed for impairment each year end or more frequently if events or changes in circumstances indicate that the asset may be impaired. The test for impairment is conducted by comparing the book value to the fair value of the reporting entity. Impairment is charged to income in the period it occurs.

3. PLAN OF ARRANGEMENT

On July 2, 2004, as a result of the Arrangement, Cequel transferred certain oil and natural gas properties to Cyries. In exchange, the former Cequel and Progress shareholders received a total of 16,230 common shares of Cyries. As Cyries and Cequel were related parties at the time of the transaction, the transfer of assets and related liabilities was recorded at the underlying carrying value of the assets and liabilities transferred.

		Amount
Oil and natural gas assets (net of accumulated depletion and depreciation of $5,787)	$	26,895
Future income tax asset		3,839
Total assets transferred		30,734
Bank debt		(10,000)
Asset retirement obligations		(2,013)
Net assets received and common shares issued	$	18,721

(all numbers in thousands except per share amounts)

4. CORPORATE ACQUISITIONS

a) Devlan Exploration Inc.

On July 1, 2005 Cyries acquired all of the outstanding common shares of Devlan Exploration Ltd. ("Devlan") pursuant to a Plan of Arrangement. Devlan shareholders received 0.25 Cyries common shares for each Devlan common share outstanding, for a total of 8,558 Cyries shares. The business combination was accounted for using the purchase method. As part of the Arrangement, Devlan transferred certain oil and natural gas properties and $4,500 of debt to a new company, Dual Exploration Inc. ("Dual"), the shares of which were distributed to shareholders of Devlan on the basis of 0.5 of a Dual share for each Devlan share outstanding.

The acquisition was funded by the issuance of common shares. The trading price ascribed to the common shares of $9.52 per share is based on the trading prices of Cyries common shares on the five days following and five days prior to the announcement of the Arrangement.

		Amount
Consideration:		
Common shares	$	81,469
Transaction costs		372
		81,841
Allocated to:		
Current assets		9,602
Current liabilities		(12,680)
Bank debt		(19,208)
		(22,286)
Property, plant and equipment		70,512
Goodwill		49,745
Asset retirement obligations		(3,560)
Future income taxes		(12,570)
	$	81,841

b) 1181608 Alberta ULC

Pursuant to a share purchase agreement, Cyries acquired all of the outstanding common shares of 1181608 Alberta ULC a private oil and natural gas exploration and production company, for cash consideration of $57,000. The acquisition closed on August 12, 2005.

		Amount
Consideration:		
Cash	$	57,000
Transaction costs		93
		57,093
Property, plant and equipment		54,717
Goodwill		18,689
Asset retirement obligations		(1,249)
Future income taxes		(15,064)
	$	57,093

The results of operations of both companies are reflected in Cyries' earnings from the respective closing dates.

(all numbers in thousands except per share amounts)

5. PROPERTY, PLANT AND EQUIPMENT

	December 31, 2005	December 31, 2004
Petroleum and natural gas property and equipment	$ 297,046	$ 65,638
Other	105	27
	297,151	65,665
Accumulated depletion and depreciation	(32,138)	(8,743)
Net book value	$ 265,013	$ 56,922

In determining the Company's depletion and depreciation, $18,715 (2004 - $4,216) of costs related to unproved properties and $13,375 (2004 - $3,661) of estimated salvage value was excluded from the costs subject to depletion. Future development costs required to complete wells for which proved reserves have been assigned of $10,600 (2004 - $2,083) were added to the Company's net book value for purposes of the depletion calculation. The Company does not capitalize corporate general and administrative expenses.

The Company performed a full cost impairment test at December 31, 2005 to assess the recoverability of its petroleum and natual gas interest. As at December 31, 2005 there was no impairment required. For purposes of the full cost impairment test, the Company used the benchmark reference prices summarized in the table below:

Year	WTI ($US/bbl)	AECO ($Cdn/mcf)
2006	57.00	10.60
2007	55.00	9.25
2008	51.00	8.00
2009	48.00	7.50
2010	46.50	7.20
Escalate thereafter	46.85	7.17

6. INCOME TAXES

The difference between the expected tax provision and the reported income tax provision is summarized below:

	Year ended December 31, 2005	Period ended December 31, 2004
Earnings before tax	$ 27,824	$ 2,549
Enacted tax rate	37.62%	38.62%
Computed income taxes at the enacted rate	10,467	984
Increase (decrease) in taxes resulting from:		
Non-deductible crown payments	5,795	635
Resource allowance	(5,008)	(623)
Income tax rate changes	(1,635)	(139)
Income tax audit adjustments	1,798	-
Non-deductible stock compensation and other	1,401	-
Capital taxes	252	-
Other	(78)	141
Provision for income taxes	$ 12,992	$ 998

(all numbers in thousands except per share amounts)

The components of future income tax are as follows:

	December 31, 2005	December 31, 2004
Tax basis in excess of property, plant and equipment carrying value	$ (40,001)	$ 2,030
Asset retirement obligation liability	4,667	847
Share issue costs	1,947	380
Other	229	10
Future income tax (liability) asset	$ (33,158)	$ 3,267

During 2005, an income tax audit was performed on certain Devlan Exploration Inc. tax filings. As a result of this audit, current tax expense includes a charge of $1,798 and future tax includes an expense of $30 due to tax pool adjustments. Estimated interest of $607 is included in interest expense.

7. REVOLVING DEMAND LOAN

The Company has a demand revolving operating credit facility provided by a Canadian chartered bank. The credit facility is limited to $73 million and provides that advances may be made by way of direct advances or bankers' acceptances. Direct advances bear interest at the bank's prime lending rate plus a variable rate and bankers' acceptances bear interest at the applicable bankers' acceptances rate plus a variable rate stamping fee. The variable rate charged by the bank is dependent upon the Company's debt to trailing cash flow ratio. As at December 31, 2005 the variable rate being charged to the Company is nil for prime loans and 1.15% for the variable rate on the stamping fees for bankers' acceptances. The credit facility is subject to periodic review and is secured by a $100 million demand fixed and floating charge debenture over all of the Company's assets.

8. SHARE CAPITAL

Authorized

At December 31, 2005, the Company had authorized an unlimited number of common shares, an unlimited number of preferred shares, 3,988 warrants and 605 Class B performance shares.

(all numbers in thousands except per share amounts)

Issued

The Company had the following shares outstanding at December 31, 2005:

Common shares	Number of shares		Amount
Issued on transfer of assets *(note 3)*	16,230	$	18,721
Initial private placement, June 28, 2004	3,988		5,065
Private placement, July 28, 2004	4,000		22,000
Share issue costs	-		(1,212)
Tax effect of share issue costs	-		426
Common shares December 31, 2004	24,218	$	45,000
Private placement, February 3, 2005	2,440		20,008
Acquisition of Devlan, July 1, 2005	8,558		81,469
Private placement August 11, 2005	4,017		50,005
Exercise of stock options	10		76
Exercise of warrants	20		40
Exercise of performance shares	2		1
Share issue costs	-		(3,528)
Tax effect of share issue costs	-		1,229
Common shares December 31, 2005	39,265	$	194,300

Warrants	Number of warrants		Amount
Initial private placement - June 28, 2004	3,988	$	1,435
Balance - December 31, 2004	3,988	$	1,435
Exercise of warrants	(20)		(7)
Balance - December 31, 2005	3,968	$	1,428

Performance shares	Number of performance shares		Amount
Initial private placement - July 28, 2004	605	$	6
Balance - December 31, 2004	605	$	6
Exercise of performance shares	(2)		-
Cancellation of performance shares	(4)		-
Balance - December 31, 2005	599	$	6

Equity issues

	Date of issue	Price per share of issue	Shares issued		Gross proceeds
Common shares	June 28, 2004	$1.27	3,988	$	5,065
Common shares	July 28, 2004	$5.50	4,000		22,000
Common shares	February 3, 2005	$8.20	2,440		20,008
Common shares	July 1, 2005	$9.52	8,558		81,469
Common shares	August 12, 2005	$12.45	4,017		50,005
Total			23,003	$	178,547

On June 28, 2004 the Company issued 3,988 common shares and 3,988 warrants in conjunction with an initial private placement of its common shares. One third of the common shares purchased in the private placement became eligible for resale on each of December 31, 2004 and June 28, 2005 with the remaining one third becoming eligible on June 28, 2006.

Each warrant is exercisable into one common share of the Company at a price of $1.63 per share until the warrants expire on June 28, 2008. One third of the warrants vest annually subject to certain performance clauses, with the initial tranche having vested June 28, 2005. In order for the initial one third and the remaining two thirds of the warrants to vest the Cyries common shares must, at any time during the term of the warrants, trade at a 20-day weighted average price of at least $2.45 and $3.26, respectively. The performance clauses have been met as of December 31, 2005. A value of $1,436 has been ascribed to the warrants for accounting purposes as determined using an option pricing model that incorporates assumptions for the vesting provisions. An expected life of 4 years, a risk free interest rate of 3.4% and a volatility of 50% were used in the pricing model.

In conjunction with the initial private placement, the Company issued 605 Class B Performance Shares to employees and directors. Each performance share was sold for a price of $0.01 per share and is convertible into the fraction of a common share equal to the closing trading price of the common shares on the Toronto Stock Exchange on the day prior to such conversion less $1.63, if positive, divided by the common share closing price. The performance shares vest at the rate of 33% per year and expire July 2, 2008. The fair value of each performance share was determined, at the date of issuance, using the Black-Scholes model. In the pricing model the fair value of the performance shares was $0.69 per share using a risk-free interest rate of 3.4%, volatility of 50% and an expected life of 3 years. The fair value of the performance shares is expensed over the vesting period of three years.

On March 2, 2005, Devlan issued flow-through shares and committed to spend $2,250 before December 31, 2005 on expenditures qualifying as Canadian exploration expenditures. These flow-through commitments were made by Devlan in March 2005. Flow-through expenditures on Canadian exploration expenses were renounced to subscribers of the flow-through common shares in February 2006 effective December 31, 2005. The related income tax impact has been recorded in the first quarter of 2006.

Share capital includes common shares of $194,300, warrants of $1,428 and performance shares of $6 for a total of $195,734.

9. STOCK BASED COMPENSATION

The Company accounts for its stock based compensation plan (the "Plan") using the fair value method. Under this method, a compensation cost is charged over the vesting period for stock options and Class B performance shares with a corresponding increase to contributed surplus.

(all numbers in thousands except per share amounts)

Stock option activity related to the Plan was as follows:

	December 31, 2005		December 31, 2004	
	Number of options	Weighted average price ($)	Number of options	Weighted average price ($)
Opening balance	460	5.41	-	-
Granted	1,222	12.03	460	5.41
Exercised	(10)	5.21	-	-
Closing balance	1,672	10.25	460	5.41

The Plan is for the benefit of employees, officers and directors. Stock options granted under the Plan vest over a four year period with 20 percent of the options vesting immediately upon grant and a further 20 percent vesting upon each anniversary date. The options expire, if unexercised, five years from the date of the initial grant. At December 31, 2005, 418 stock options have vested and the average remaining life of the outstanding stock options is 4.3 years.

The following table provides additional information on the stock options outstanding as at December 31, 2005:

Range of exercise prices ($/share)	Number of options	Weighted average exercise price	Weighted average contractual life	Options exercisable
5.21 - 6.50	450	$ 5.41	3.7	174
10.40 - 16.60	1,222	12.03	4.5	244
5.21 - 16.60	1,672	$ 9.28	4.3	418

The fair value of each stock option granted in the year ended December 31, 2005 was estimated on the date of grant using the Black-Scholes model. The weighted average fair value of the stock options granted in the year was $5.01 (2004 - $2.41) per share, using an average risk-free interest rate of 2.8 percent (2004 - 3.03 percent), average volatility of 47 percent (2004 - 50 percent) and an expected life of 4.5 years (2004 - 4.5 years). The Company has not re-priced any stock options.

For the year ended December 31, 2005, $2,042 of expense related to the stock options and $130 of expense related to the performance shares is included in stock compensation expense.

The following table reconciles the Company's contributed surplus:

	December 31, 2005	December 31, 2004
Contributed surplus, beginning of period	$ 365	$ -
Stock based compensation expense	2,172	365
Exercise of stock options	(23)	-
Exercise of performance shares	(1)	-
Cancellation of performance shares	(1)	-
Carrying amount, end of period	$ 2,512	$ 365

(all numbers in thousands except per share amounts)

10. PER SHARE AMOUNTS

The following table details the components of diluted common shares outstanding:

	Year ended December 31, 2005	Period July 2, 2004 to December 31, 2004
Weighted average common shares		
Basic	32,286	23,646
Warrants	3,469	2,983
Performance shares	527	453
Options	134	-
Diluted	36,416	27,082

The calculation of diluted common shares excludes 1,537 of stock options that are anti-dilutive.

11. ASSET RETIREMENT OBLIGATIONS

The total future asset retirement obligations were estimated by management based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon the wells and facilities and the estimated timing of the costs to be incurred in future periods. The Company has estimated the net present value of its asset retirement obligations to be $12,440 (2004 - $2,519) as at December 31, 2005 based on a total future liability of $32,249 (2004 - $6,271). Asset retirement expenditures are expected to be made over the next 25 years. The Company used a credit adjusted risk free rate of seven percent and an inflation rate of two percent to calculate the present value of the asset retirement obligation. The following table reconciles the Company's total asset retirement obligation.

	Year ended December 31, 2005	Period July 2, 2004 to December 31, 2004
Balance, beginning of period	$ 2,519	$ 2,013
Increase in liabilities	1,238	301
Liabilities settled	(80)	-
Dispositions	(365)	-
Acquisitions	5,717	-
Revisions	2,967	123
Accretion	444	82
Carrying amount, end of period	$ 12,440	$ 2,519

(all numbers in thousands except per share amounts)

12. SUPPLEMENTAL CASH FLOW INFORMATION

	Year ended December 31, 2005	Period July 2, 2004 to December 31, 2004
Changes in non-cash working capital		
Accounts receivable	$ (11,413)	$ (8,916)
Prepaid expenses and deposits	(245)	(606)
Accounts payable and accrued liabilities	28,330	15,743
Net change in non-cash working capital	16,672	6,221
Investing activities	$ 14,475	$ 8,795
Operating activities	$ 2,197	$ (2,574)

The Company made the following cash outlays in respect of interest expense and current income taxes:

	Year ended December 31, 2005	Period July 2, 2004 to December 31, 2004
Interest	$ 872	$ 7
Income taxes	$ 588	$ -

13. COMMITMENTS

The company is committed to payments under an operating lease for office space through September 2007 totaling $875 (2006 - $495; 2007 - $380).

14. FINANCIAL INSTRUMENTS

The Company's financial instruments recognized in the balance sheet consist of accounts receivable, accounts payable and the revolving demand loan. The fair value of these financial instruments approximate their carrying value due to their short term to maturity and the floating interest rate on the loan.

Risk management activities

The nature of the Company's operations result in exposure to fluctuations in commodity prices, exchange rates and interest rates. The Company monitors and when appropriate, may use derivative financial instruments to manage its exposure to these risks. For the periods presented the Company has not entered into any derivative financial instruments.

Substantially all of the Company's accounts receivable are due from companies in the oil and gas industry and are subject to the normal industry credit risks. The carrying value of accounts receivable reflects management's assessment of the associated credit risks.

/d	per day
ARTC	Alberta Royalty Tax Credit
bcf	billion cubic feet
boe	barrels of oil equivalent (6,000 cubic feet of natural gas being equivalent to one barrel of oil)
bbl	barrel of oil or natural gas liquids
mboe	thousand barrels of oil equivalent
mcf	thousand cubic feet
mmcf	million cubic feet
NGL	natural gas liquids
WTI	West Texas Intermediate

NOTES

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